The Economist

January , 2011



Politics this week

Jan 20th 2011 | from PRINT EDITION



As protests persisted across **Tunisia**, its president for the past 23 years, Zine el-Abidine Ben Ali, fled to Saudi Arabia, leaving his prime minister to try to cobble together a unity government including several former members of the opposition. It was unclear whether this would help restore calm. Several nominees refused to join the new government unless Mr Ben Ali's party was completely swept from power. Officials said 78 people had been killed in street violence in the past few weeks; the opposition said the true figure was several times higher. See article

A wave of **self-immolations**, to copy the action of a young man who sparked Tunisia's upheaval in December, took place in some Arab countries, including Algeria and Egypt. See article

Ehud Barak, a former prime minister who is the defence minister in Binyamin Netanyahu's ruling coalition in **Israel**, split from the Labour party, of which he had been the leader, to form a new party called Independence. He took four of Labour's parliamentarians with him, while the other eight left the coalition in the hope of rejuvenating the peace camp opposed to the government. See article

In the most lethal attack against the authorities in **Iraq** since November, a suicide-bomber killed at least 60 people outside a police-recruitment centre in Tikrit, Saddam Hussein's home town, north of Baghdad. The next day another suicide-bomber used an ambulance to kill at least ten people in Baquba, a city north-east of the capital.

As the polls closed in **South Sudan's** referendum on whether to secede from the north, preliminary results suggested that the yes vote would exceed 90%.

Oh, Silvio!

Italian prosecutors said they were investigating charges that **Silvio Berlusconi**, Italy's prime minister, had paid for sex with an underage Moroccan-born dancer, among others, and had abused his office by securing her release from police custody. Extracts from the dancer's wiretapped conversations were published in the press, including a comment from one woman that the prime minister had "even become ugly". Mr Berlusconi denied the allegations. See article

Brian Cowen, **Ireland's** beleaguered prime minister, survived a confidence vote in his leadership of Fianna Fail, the main governing party. He will now lead his party into a general election, probably in March, at which it is expected to take a pounding. See article

At a meeting of **euro-zone** ministers in Brussels, Germany's finance minister, Wolfgang SchÃ¤uble, squashed hopes of an immediate relaxation in the rules governing the use of the euro440 billion ($593 billion) rescue fund created last May. The European Commission had earlier called for an increase in its lending capacity.

It emerged that British and Russian police were investigating the activities of four Russian government officials assigned to the **European Bank for Reconstruction and Development**. The bank said it had lifted immunity from prosecution for the four.

United we sit

Doctors took congresswoman Gabrielle Giffords off the critical list, though she remains in a serious condition. After the Tucson shootings, and a well-received speech by Barack Obama calling for more **civility** in American politics, congressmen made an effort to tone down the rhetoric; some even urged their colleagues to abandon the usual party seating divisions at next week's state-of-the-union address.

Republicans in the House voted to overturn last year's **health-care-reform** act. The measure was largely symbolic and has no chance of advancing, but the party has vowed to introduce a steady drip of further bills to dismantle the reforms.

Reince Priebus won a ballot to become the chairman of the **Republican** national party, ending the gaffe-laden tenure of Michael Steele.

Some old hands in the **Senate** decided not to seek re-election in 2012: Joe Lieberman, who was Al Gore's running mate in 2000 but has since occasionally antagonised Democrats, notably over his staunch support for the Iraq war; Kent Conrad, a Democrat from North Dakota; and Kay Bailey Hutchison, a Republican from Texas.

The eagle dances with the tiger



Hu Jintao visited America. After a fractious few months that have brought differences to the fore over arms build-ups, currency policy and other issues, the Chinese president and his American counterpart were at pains to stress the benefits of the relationship between the two countries. **China** agreed to $45 billion in trade and investment contracts during the trip. Mr Hu said that China and America should "respect each other's choice of development path".

Hamid Karzai, **Afghanistan's** president, agreed to a request by a special election court to delay the inauguration of a new parliament until February 22nd, to give it more time to investigate allegations of fraud at last year's election.

The Communist Party in **Vietnam** wrapped up an important congress with an apology by the outgoing party chief for mishandling the economy. Yet the prime minister kept his job.

The Association of South-East Asian Nations called on Western countries to lift sanctions on **Myanmar**, now that Aung San Suu Kyi was free and a parliament about to convene.

What's Doc up to?



Jean-Claude "Baby Doc" Duvalier, a former dictator, returned unexpectedly to **Haiti**, where he was questioned by prosecutors who charged him with embezzlement and corruption before releasing him. A judge will now consider whether there is enough evidence to warrant a trial. Mr Duvalier's return coincides with a dispute over the result of a presidential election. Another exiled president, Jean-Bertrand Aristide, promptly said he too wants to return. See article

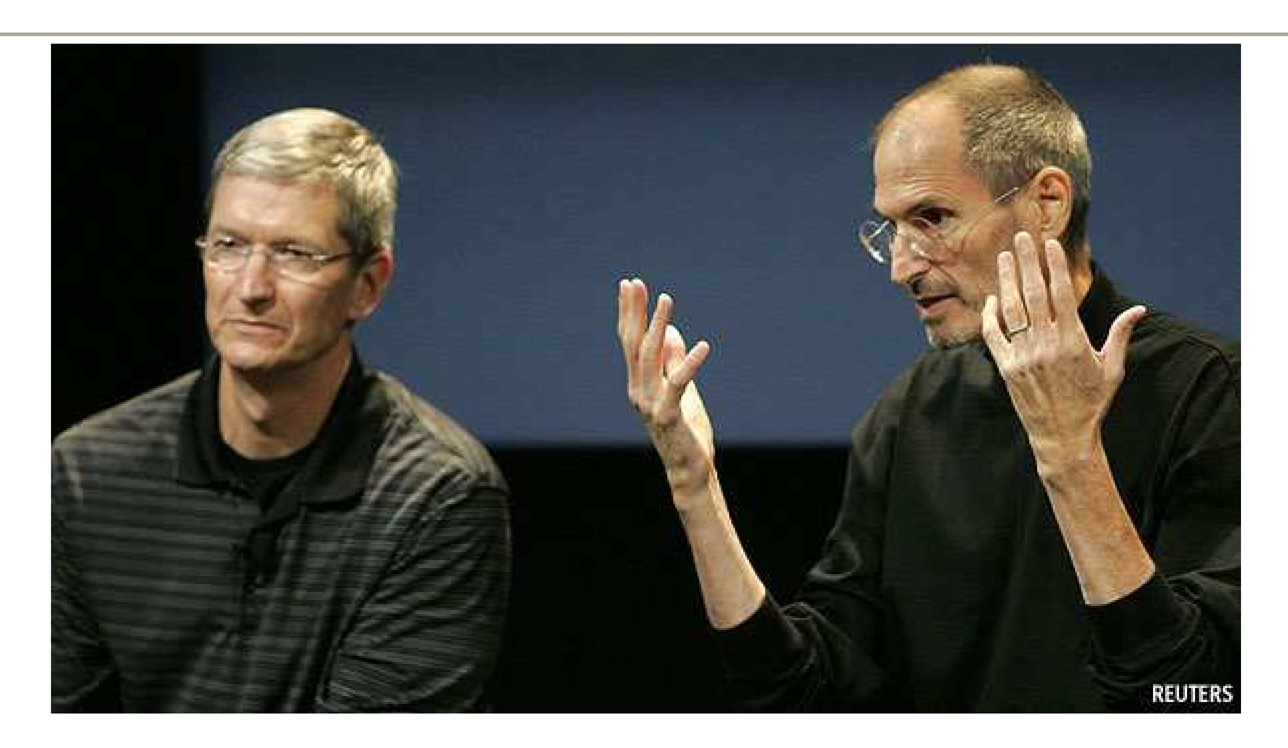
Barack Obama's administration relaxed restrictions on travel to **Cuba** by academic, religious and cultural groups and indicated that it would permit more charter flights to the island. Americans will now be allowed to send money to Cubans to support "private economic activity". See article

The death toll from the recent flooding and mud landslides in towns located near the mountains behind **Rio de Janeiro** rose to at least 740. Another 21,500 people have been left homeless. See article

---

Business this week

Jan 20th 2011 | from PRINT EDITION



Steve Jobs (pictured right) worried investors in Apple by taking immediate medical leave, the chief executive's second such absence in less than two years. Mr Jobs was diagnosed with cancer in 2003, though he did not reveal his condition for nine months, and had a liver transplant in 2009, which was reported three months after the operation. No reason was given for his taking leave this time. See article

Meanwhile, **Apple** posted another strong set of quarterly earnings. In the three months before Christmas it sold 16.2m iPhones, almost twice as many as a year earlier, and 7.3m iPads, around 20% more than had been expected. Sales of iPods were 7% lower, at 19.5m.



Higher gas bills, more expensive air fares and the rising cost of food, notably vegetables and cereals, were factors behind an unexpected jump in Britain's **inflation rate** for December, to 3.7%, another consideration for the Bank of England as it ponders whether to raise interest rates this year. See article

In **China** the rate of inflation in December stood at 4.6%, lower than November's 28-month high of 5.1% and easing some of the pressure on the government over politically sensitive price rises. China's GDP grew by 9.8% in the fourth quarter from a year earlier, a more rapid pace than was expected. The economy expanded by 10.3% for the whole of 2010.

Brazil raised its benchmark interest rate, already the highest among big economies, by 50 basis points, to 11.25%, to combat surging inflation.

In an embarrassing turnaround **Goldman Sachs** said it would restrict participation in the investment vehicle it has set up to buy equity in privately held **Facebook** to its clients outside America. The large amount of publicity that the offer generated inside America could potentially have run foul of securities law. See article

Entering deep waters

BP and **Rosneft** struck a deal that sees BP increase its stake in Rosneft from 1.3% to 10.8% and the Russian state-owned energy firm take a 5% holding in BP. The pair also set up a venture to explore oil and gas deposits beneath Russia's Arctic shelf. The agreement marks a step for BP in moving on from last year's oil-spill disaster. However, some American politicians raised concerns about BP, which has many assets in America and supplies fuel to the military, working so closely with a Russian company. One congressman quipped that "BP once stood for British Petroleum...it now stands for Bolshoi Petroleum." See article

The International Energy Agency raised its forecast of the world's demand for **oil** this year and warned that economic recovery could be hampered by oil prices, which are at their highest level in more than two years. See article

People just love to fly

Virgin America announced that it placed a firm order late last year for 60 **Airbus** A320 jets, including 30 A320 NEOs, tripling its fleet as it expands its routes in North America. It will be the first carrier to fly the more fuel-efficient NEO version of the A320. The order is another boost for Airbus, after a record purchase of jets from an Indian airliner, and vaults the European aircraft-maker ahead of **Boeing** for orders in 2010. Boeing got a lift, however, with the announcement during Hu Jintao's visit to Washington that China would buy an extra 200 of its planes.

Cargill, America's biggest privately held company, decided to spin off **Mosaic**, a leading producer of potash and phosphate, in which it holds a 64% stake. The transaction is valued at $24 billion and will cheer the charitable trusts that were established by the granddaughter of Cargill's founder; they have long sought to gain value from the shares they hold. With food prices soaring, pushing up the demand for fertiliser, Mosaic may make an attractive takeover target for the likes of BHP Billiton.

A lawyer for one of the three executives sacked by **Renault** in an alleged case of industrial espionage said his client would challenge his dismissal through a tribunal. Michel Balthazard headed the carmaker's pre-engineering projects team. Another of the sacked three launched a lawsuit against the carmaker. Renault has filed a complaint with the state prosecutor in Paris "against persons unknown" after the discovery of "misconduct detrimental to the company", rumoured to be a leak (or sale) of its electric-car technology to another country.

Grin and Baer it

At a press conference in London, a former banker at the Cayman Islands offices of Julius Baer, a Swiss bank, handed over a second batch of confidential data to Julian Assange, the founder of WikiLeaks, relating to 2,000 accounts. Rudolf Elmer was fired by Baer in 2002, and now says he wants to expose tax evasion. Later in the week a court in Switzerland fined Mr Elmer for breaching **banking-secrecy** laws in a prior disclosure of documents. He was arrested soon after leaving the court.

Index | The world this week

Daily Chart

Jan 20th 2011 | From *The Economist* print edition



Inequality

The rich and the rest

Jan 20th 2011 | from PRINT EDITION

What to do (and not do) about inequality



APART from being famous and influential, Hu Jintao, David Cameron, Warren Buffett and Dominique Strauss-Kahn do not obviously have a lot in common. So it tells you something about the breadth of global concerns about inequality that China's president, Britain's prime minister, America's second-richest man and the head of the International Monetary Fund have all worried, loudly and publicly, about the dangers of a rising gap between the rich and the rest.

Mr Hu puts the reduction of income disparities, particularly between China's urban elites and its rural poor, at the centre of his pledge to create a "harmonious society". Mr Cameron has said that more unequal societies do worse "according to almost every quality-of-life indicator". Mr Buffett has become a crusader for a higher inheritance tax, arguing that America risks an entrenched plutocracy without it. And Mr Strauss-Kahn argues for a new global growth model, claiming that gaping income gaps threaten social and economic stability. Many others seem to share their concerns. A new survey by the World Economic Forum, whose annual gathering of bigwigs in Davos begins on January 26th, says its members see widening economic disparities as one of the two main global risks over the next decade (alongside failings in global governance).

Equally muddled

The debate about inequality is an old one. But in the wake of a financial crisis that is widely blamed on Wall Street fat cats, from which the richest have rebounded fastest, and ahead of public-spending cuts that will hit the poor hardest, its tone has changed. For much of the past two decades the prevailing view among the world's policy elite-call it the Davos consensus-was that inequality itself was less important than ensuring that those at the bottom were becoming better-off. Tony Blair, a Labour predecessor of Mr Cameron's, embodied that attitude. His New Labour party was famously said to be "intensely relaxed" about the millions earned by David Beckham (a footballer) provided that child poverty fell.

Now the focus is on inequality itself, and its supposedly pernicious consequences. One strand of argument, epitomised by "The Spirit Level", a book that caused a stir in Britain, suggests that countries with greater disparities of income fare worse on all manner of social indicators, from higher murder rates to lower life expectancy. A second thread revisits the macroeconomic consequences of income disparities. Several prominent economists now reckon that inequality was a root cause of the financial crisis: politicians tried to counter the growing gap between rich and poor by encouraging poorer folk to take on more credit (see article). A third argument is that inequality perverts politics, with Wall Street's influence in Washington often cited as exhibit A of the unhealthy clout of a plutocratic elite.

If these arguments are right, there might be a case for some fairly radical responses, especially a greater focus on redistribution. In fact, much of the recent hand-wringing about widening inequality is based on sloppy thinking. The old Davos consensus of boosting growth and combating poverty is still a better guide to good policy. Rather than a sweeping assault on inequality itself, policymakers would do better to take on the market distortions that often lie behind the most galling income gaps, and which also impede economic growth.

Begin with the facts about inequality. Globally, the gap between the rich and the poor has actually been narrowing, as poorer countries are growing faster. Nor is there a monolithic trend within countries (see article). In Latin America, long home to the world's most unequal societies, many countries-including the biggest, Brazil-have become a bit more equal, as governments have boosted the incomes of the poor with fast growth and an overhaul of public spending to improve the social safety-net (but not by raising tax rates for the rich).

The gap between rich and poor has risen in other emerging economies (notably China and India) as well as in many rich countries (especially America, but also in places with a reputation for being more egalitarian, such as Germany). But the reasons for this differ. In China inequality has a lot to do with the *hukou* system of residency permits, which limits internal migration to the towns; by some measures inequality has peaked as rural labour becomes more scarce. In America income inequality began to widen in the 1980s largely because the poor fell behind those in the middle. More recently, the shift has been overwhelmingly due to a rise in the share of income going to the very top-the highest 1% of earners and above-particularly those working in the financial sector. Many Americans are seeing their living standards stagnate, but the gap between most of them has not changed all that much.

The links between inequality and the ills attributed to it are often weak. For instance, some of the findings in "The Spirit Level" were distorted by outliers: strip out America's high murder rate (which many would blame on guns, not inequality) or Japan's longevity (diet, not equality), and flatter societies no longer look so much healthier. As for the mooted link to the financial crisis, the timing is dodgy: America's poor fell behind in the 1980s, the credit bubble took off two decades later.

Message to Davos

These nuances suggest that rather than fretting about inequality itself, policymakers need to differentiate between its causes and focus on ways to increase social mobility. A global market offers far bigger returns to those at the top of their game, be they authors, lawyers or fund managers. Modern technology favours the skilled. These economic changes are themselves often reinforced by social ones: educated men now tend to marry educated women. The result of all this, as our special report this week shows, is the rise of a global elite.

At heart, this is a meritocratic process; but not always. Rules and institutions are often rigged in ways that limit competition and favour insiders at the expense both of growth and equality. The rules can be blatantly unfair: witness China's limits to migration, which keep the poor in the countryside. Or they can involve more subtle distortions: look at the way that powerful teachers' unions have stopped poorer Americans getting a good education, or the implicit "too big to fail" system that encouraged bankers to be reckless and left the rest with the tab. These are very different problems, but they all lead to wider inequality, fewer rungs in the ladder and lower growth.

Viewed from this perspective, the right way to combat inequality and increase mobility is clear. First, governments need to keep their focus on pushing up the bottom and middle rather than dragging down the top: investing in (and removing barriers to) education, abolishing rules that prevent the able from getting ahead and refocusing government spending on those that need it most. Oddly, the urgency of these kinds of reform is greatest in rich countries, where prospects for the less-skilled are stagnant or falling. Second, governments should get rid of rigged rules and subsidies that favour specific industries or insiders. Forcing banks to hold more capital and pay for their implicit government safety-net is the best way to slim Wall Street's chubbier felines. In the emerging world there should be a far more vigorous assault on monopolies and a renewed commitment to reducing global trade barriers-for nothing boosts competition and loosens social barriers better than freer commerce.

Such reforms would not narrow all income disparities: in a freer world skill and intellect would still be rewarded, in some cases magnificently well. But the reforms would strike at the most pernicious, unfair sorts of income disparity and allow more people to move upwards. They would also boost growth and leave the world economy more stable. If the Davos elites are worried about the gap between the rich and the rest, this is the route they should follow.

Index | Leaders

China's currency

The rise of the redback

Jan 20th 2011 | from PRINT EDITION

China will have to open its financial market if it wants the yuan to rival the dollar



IN 1965 Valery Giscard d'Estaing, then France's finance minister, complained that America, as the issuer of the world's reserve currency, enjoyed "an exorbitant privilege". China's president, Hu Jintao, does not have quite the same way with words. But on the eve of his visit to America this week he told two of the country's newspapers that the international currency system was a "product of the past". Something can be a product of the past without being a thing of the past. But his implication was clear: the dollar's role reflects America's historical clout, not its present stature.

Mr Hu is right that America's currency punches above its economy's diminished weight in the world. America's share of global output (20%), trade (only 11%) and even financial assets (about 30%) is shrinking, as emerging economies flourish. But many of those economies, such as South Korea, still sell their exports for dollars; many, including China, still peg their currencies to the greenback, however loosely; and about 60% of the world's foreign-exchange reserves remain in dollars.

This allows America to borrow cheaply from the rest of the world. Its government has been able to overspend, secure in the knowledge that its IOUs will be bought by foreign central banks, which are not too fussy about price. America would show more self-discipline, many Chinese believe, if the dollar had a little bit more competition.

Could the yuan become a rival? China's economy will probably surpass America's in outright size within 20 years. It is already a bigger exporter. It is prodding firms to settle trade and even acquire foreign companies in its own currency. That is adding to a pool of "redbacks" outside its borders. These offshore yuan are, in turn, being tapped by borrowers, issuing "dim sum" bonds in Hong Kong (see article).

But as the dollar's history shows, economic clout is not enough without financial sophistication (see article). If foreigners are to store their wealth in yuan, they will need financial instruments that are safe, stable and easily sold. Dim sum makes for a tasty appetiser. But the main feast of China's financial assets is onshore and off-limits, thanks to its strict capital controls. The government remains deeply reluctant to let foreigners hold, buy and sell these assets, except under tight limits. Indeed, it is barely ready to give its own people financial freedom: interest on bank deposits is capped; shares are largely owned by state entities; and bonds are chiefly held by the banks-which are, in turn, mostly owned by the state.

Over time China will relax its financial grip. But even if it could usurp the dollar's role as the world's currency, it will not replicate the American set-up. The United States takes advantage of the dollar's position to borrow cheaply from the rest of the world, selling its assets in return for goods. China is a mirror image of this. It runs a trade surplus, selling goods in return for financial claims on foreigners. Its firms, households and government save more than they can invest at home.

A different kind of perk

Rather than seeking to borrow in its own currency, China may harbour the opposite ambition: to lend in its own currency. The exorbitant privilege it may covet is a lower foreign-exchange risk on its savings. On top of the trillions China has lent to America's treasury, it also holds stakes in Australian mines, African farms and Swedish car companies. But because none of these assets is in yuan, China suffers a capital loss whenever its currency strengthens. It would no doubt like to share some of this risk with the rest of the world. The model is not America, but Germany, an international creditor which holds 70% of its foreign assets in euros.

There is a catch, though. No one will want to borrow in a currency that is only ever going to strengthen, increasing the value of their debts. So if China wants to "yuanify" some of its claims on the rest of the world, it will need a currency that can go down as well as up. To make people believe the yuan can fall tomorrow, China will have to loosen its currency's peg and let it rise faster today. China is different from America: it is a rising economic power and a thrifty one. But one rule still holds: China will have to open its financial system to the world if the yuan is to be the dominant currency.

Index | Leaders

Tunisia and the Arab world

Let the scent of jasmine spread

Jan 20th 2011 | from PRINT EDITION

How wonderful if Tunisia became a paragon of democracy for other Arab countries to emulate



TO SEE an Arab country shaking off the shackles of despotism is a rare and unalloyed joy. Moreover, Tunisia has a chance to set an example for the rest of the Arab world. It is a small country which, for all the venality of its ousted leader, Zine el-Abidine Ben Ali, has done better than most at opening up to the world, getting its economy to grow apace, educating its 10.6m people, giving them a modicum of health, and promoting its women. The bearded fanatics who have all too often been spawned by repressive regimes as the vanguard of opposition seem mercifully absent from the streets of Tunis. If calm is restored and genuine elections take place in the next few months, Tunisia may yet emerge as a pluralist and peaceful democracy. It would be a momentous event.

It would also be a beacon. Among the Arab League's 22 countries, only three can claim to be democracies and all of those are flawed: Iraq, still afflicted by suicide-bombers and sectarianism, its democracy forced on it by the United States; the Palestinian territories, a state as yet only in name, occupied by Israel and contested by its own people; and Lebanon, where free elections are marred by the necessity of sectarian quotas and where the nation is torn between conflicting visions that, even in the past fortnight, have deprived it of a government. All the rest range from the nastiest of tyrannies, such as Libya's, to the more benevolent autocracies, such as Qatar's, with shades of authoritarian and oligarchic regimes in between. Yet none gives its people the right to choose who will run their lives. The Arab world embraces vast wealth and more than 350m people. One of the great puzzles is why in terms of democracy it should be the most backward on earth.

Nothing suggests that Arabs are inherently disposed to reject the ballot box. Nor is the practice of Islam, at least in its more malleable versions, incompatible with multiparty democracy. Here Turkey has shown the way, with a mildly Islamist ruling party accepting constitutional checks and balances, including in matters of mosque and state. Mainly Muslim Asian countries, such as Malaysia and Indonesia, are also seeking to entrench democratic systems. Even Iran under the ayatollahs had, before the repression of the past 18 months or so, tolerated more political competition and open debate than its Arab neighbours have.

Don't jump the Tunisian gun...

However, the "jasmine revolution" has a long way to go before it can claim to have established a democracy (see article). The fall of Mr Ben Ali was fairly bloodless and astonishingly sudden. His successors, such as they are, have promised the release of all political prisoners, the freedom of the press, the legality of all political parties and the holding of genuine elections under the gaze of international observers. But such early gains are still reversible. Nobody knows who, in a week's time, will be in control. Chaos may persist. Leading figures from Mr Ben Ali's regime are still in contention. His hated security service seems to be pitted against the more respected army, which could yet step in-initially with popular support, if it stems the flow of blood on the streets. The opposition is inchoate, its leadership unknown, its aims so far vague and various.

Leaders in the rest of the Arab world are nervous-and so they should be. The mobile telephone, satellite television and the internet all have the potential to weaken their capacity for keeping their people in the dark and under their control. The cannier despots know that whispers of dissent among the few can turn into howls of anger among the many-in a Tunisian trice. Across the Maghreb-in Morocco and Algeria to the west and Libya and Egypt to the east-the din of Tunisian protests is reverberating. With its 84m mostly poor and frustrated people, Egypt is the pivot. It is the main ally of the West and a

force for moderation in the search for peace between Israel and the Palestinians. If it should implode, the geopolitics of the entire Middle East would be turned upside down.

But do not assume that the heady scent of jasmine will dispatch the rest of the region's despots. The Arab world is not like eastern Europe two decades ago, when repressive regimes tumbled because ordinary people suddenly dislodged the prop of Soviet power. Today's Arab leaders have long relied on their own home-grown security systems. They will not relinquish any control in a hurry. Autocrats know that opening the door to democracy a bit risks letting the mutinous masses barge the whole way in.

Moreover, the spectre of Islamism-not to be confused with plain Islam-makes many observers queasy. Tunisia's new wave so far is secular. But what if an Islamist movement, here and there in the region, rose on the crest of revolt-and took power by the ballot box? Would it allow "one person, one vote, one time", as many secular critics predict? For too long this fear has made Western governments look the other way when secular but repressive Arab regimes, helping to swat the jihadists, have denied their people basic freedoms.

...and don't fear Islam

It is not an easy calculation. Many Islamists think God and the Koran should take precedence over parliaments, parties, pluralism and popular debate. At the extreme end of the Islamist spectrum are hard men whose rule would be a lot harsher than that of Mr Ben Ali and his ilk. But in few Arab countries is an extreme version of Islam either preponderant or popular. The Muslim Brotherhood, the true opposition in Egypt, embraces a range of attitudes. The more tolerant and sensible in its number are probably the most popular. Seeing that undemocratic secular regimes have failed to give them satisfaction, Arabs should be allowed to vote for Islamists if that is their wish. It is a risk-for themselves and for the rest of the world. However, as the past few weeks have shown, winking at secular despots, as they tighten the screws on their disgruntled people, may in the long run be riskier.

Tunisia's upheaval has only just begun. No one knows where it will lead. It has already opened an Arab Pandora's box. Frightening things may yet leap out. But it nonetheless deserves an enthusiastic welcome.

Index | Leaders

Asian medical innovation

Life should be cheap

Jan 20th 2011 | from PRINT EDITION

How China and India can help cut Western medical bills



ACROSS the rich world, governments with ageing populations are worried about soaring health-care costs. In Britain this week David Cameron announced yet another reorganisation of the National Health Service (see article). But the problem is most severe in America. Medical spending per head has nearly tripled since 1990, yet most indicators of health have barely budged. And the rising cost of health care depresses wages-because many Americans receive health insurance from their employers, who therefore pay them less.

Help may be at hand. Frugal innovators in China and India are making medical devices that are cheaper-sometimes by an order of magnitude-than their Western equivalents. Companies such as China's Mindray and India's TRS serve home markets that include vast numbers of people for whom every yuan or rupee counts. So these companies focus relentlessly on reducing costs. They create products that are stripped to their essentials: scanners that cost $10,000 rather than $100,000; portable electrocardiographs that cost $500 instead of $5,000 (see article).

These devices are not merely cheap knock-offs of Western designs. Often they are just as effective as the gold-plated kit used in the West, yet they are rarely found in rich-world hospitals. Their absence helps explain the massive disparity in costs between Western and emerging-world treatments. A night in an American hospital typically costs 25 times as much as a night in an Indian, Brazilian or Chinese one; a night in a European hospital typically costs four times as much.

Western medical-device firms are well aware of eastern innovation. Indeed, firms such as GE Healthcare, Philips and Medtronic are investing heavily in China and India: setting up research centres, hiring local talent and developing frugal inventions of their own, which they gleefully sell both locally and in other emerging markets. Alas, they are not rushing to market such thrifty ingenuity back in America or Europe.

Two main factors keep cheap devices out of Western markets. One is the muting of price signals. Health care is not an efficient market in the rich world because-be it in Europe, where the state typically pays the bills, or in America, where private insurance companies do-the customer does not have to shop around. Patients neither know nor care how much anything costs, so they demand the best of everything, which is wonderful for the makers of hugely expensive equipment.

A second factor-which applies more in America than in Europe-is red tape. America's Food and Drug Administration (FDA) is excessively risk-averse: it often takes twice as long to approve a new medical technology as European regulators do. America's confusing approvals process deters upstart medical-technology firms, since they typically lack the deep pockets and army of experts required to navigate it. And for a device to succeed in America it must be blessed not just by the FDA but also by the bureaucrats who oversee Medicare and Medicaid, the two huge government health-care schemes. Obtaining that blessing can take years.

Frugally does it

Just as the appearance of cheap, well-engineered Japanese cars disrupted Western car markets, so the rise of frugal technology could transform the market for medical devices. Western politicians need to encourage this to happen. By turning their governments into better purchasers and by eliminating the barriers that discourage the sale of cheap technology in the rich world, they could bring down the cost of health care. That should earn them the gratitude of patients, taxpayers and workers-in other words, voters.

Doing deals in Russia

How bad is BP?

Jan 20th 2011 | from PRINT EDITION

Russia is an unsavoury place to do business; that does not make BP's Russian deal wrong



VLADIMIR PUTIN has a wry sense of humour. Commenting on the new tie-up between BP, a British oil firm, and Rosneft, a Russian state-controlled one, he remarked that "one who has been beaten is worth two who haven't." That could refer to the reputational battering BP recently sustained after its disaster in the Gulf of Mexico, or to BP's experiences in Russia. In 2008 Bob Dudley, then boss of TNK-BP, a joint venture set up in 2003 to pump Siberian oil, had to flee Russia amid what he called "sustained harassment" from his hosts.

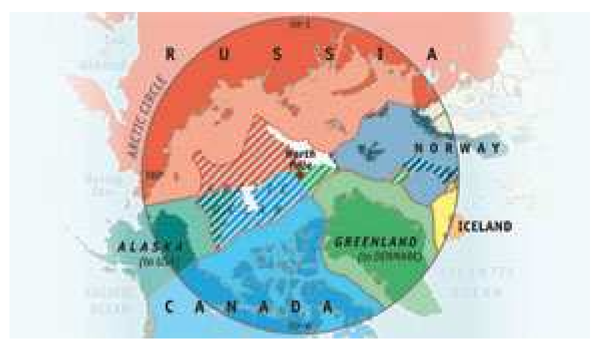
Yet BP has done well out of Russia: TNK-BP is now a thriving business that contributes an eighth of the British giant's profits (and Mr Dudley, pictured left shaking hands with Rosneft's boss, now runs the British oil giant). But Mr Putin's casually thuggish comment, and the fuss that the deal has caused, point to an underlying problem for businesspeople: should a responsible company climb into bed with a dodgy one?

Rosneft is a brazen example of Mr Putin's crony state capitalism (see article). Its main asset was grabbed from Yukos, a private firm destroyed by the Kremlin in 2004-its boss, Mikhail Khodorkovsky, was too independent-minded for Mr Putin's taste and was thrown into jail. And this is a deal not just to buy or distribute oil but to swap ownership stakes. BP's critics say it legitimises theft (right after Mr Khodorkovsky's sentence had been extended by another seven years) and bolsters the belief in the Kremlin that Western business people are really just as greedy and cynical as its own oligarchs: all that high-mindedness over corruption and property rights melts away whenever Russia dangles an oily profit in front of them.

This newspaper is no fan of Mr Putin, and has warned Western companies of the perils of dealing with him. After Yukos's dismemberment, we advised investors not to buy Rosneft's shares when it was allowed to list on the London Stock Exchange. But BP is surely free to weigh the merits of a deal.

Caesar, God and the politicians

The energy business does not reward squeamishness. From Arabia to Africa, it is dominated by unsavoury state firms. If the American politicians making jokes about Bolshoi Petroleum applied the same standards to other countries and their own companies, their cars would have run out of gas long ago.



Watch our

But there is a stronger argument than the difficulty of maintaining high standards in a dodgy industry: the division of responsibility between corporate and political actors. A company's job is to make money for its shareholders legally. Morality is the province of private individuals and of governments. BP's move will certainly make it harder for Western politicians to handle Mr Putin. But if they want to stop companies from doing deals with Mr Putin's mob-or to be diverse, or charitable, or nice-they should pass laws, not make speeches.

Opponents of shareholder capitalism claim that it is unscrupulous. Yet good behaviour is usually good business. BP's deal may turn out to be a rotten one because of Rosneft's dodgy origins. Yukos's disgruntled former shareholders are pursuing Russia through international courts with claims for nearly $100 billion. BP will surely be dragged into this mess. And Mr Putin's friends may decide that the British firm is worth another spot of "sustained harassment".

BP is betting that Russia needs its expertise; that the Russian state is less likely to sabotage a joint venture in which it has a stake; and that because this is the first deal of its kind, the Russian government needs to make it work. So the deal is a gamble-but one that BP's managers are entitled to take.

Index | Leaders

The costs of drug prohibition

Let them chew coca

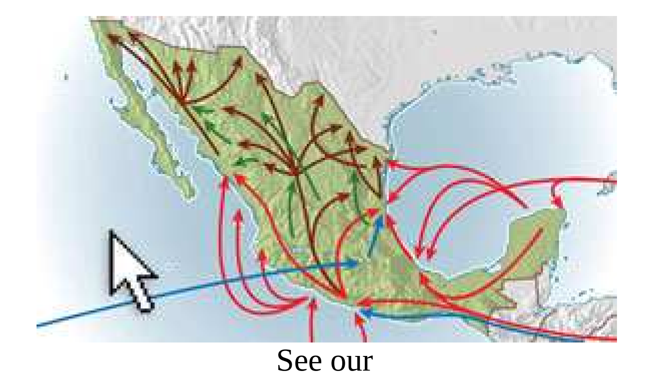
Jan 20th 2011 | from PRINT EDITION

Beware talk of victory in Latin America's drug wars



LOOKED at in one way, Mexico's drug warriors have cause for satisfaction. Over the past year or so its security forces have captured or killed 20 of the three dozen leaders of the cartels which dominate the business of supplying cocaine to the many Americans who like to consume it. The latest to fall was a founder of the Zetas, a particularly vicious mob, arrested this week. Until recently the drug barons could rely on tip-offs from corrupt police commanders, which is why they were able to turn parts of northern Mexico into private fiefs. Nowadays when the United States passes on real-time intelligence on the mobsters, the Mexicans-frequently marines, but sometimes even the federal police-tend to nab their man.

That counts as progress. But it has come at a fearsome cost. Taking out the *capos* unleashes bloody turf wars. With over 15,000 killed, 2010 was by far the bloodiest year in Mexico since Felipe Calderon took office as president in December 2006 and launched his crackdown on the drug gangs. Officials argue that the death toll has begun to fall, that nearly all of the dead are gangsters, and that the killings are confined to a few hot spots. But it is too early to conclude that the fall marks a turning-point. And the government's critics point out that a worrying number of the victims have been innocent bystanders. As the violence spreads to previously calm areas, the average Mexican feels less safe. Public support for Mr Calderon's crusade is flagging and the gains he has made may yet be lost.



See our

This suggests that Mr Calderon has got his priorities wrong. Better everyday policing should have accompanied the elite anti-drug spearhead. Local forces need wholesale change, and the federal force should be both bigger and better.

But even if Mr Calderon can reform the police, there is a second cost to his drug war. With their leaders under fire, the drug combines are moving into the poorer countries of Central America (see article). There, governments are even less equipped to deal with the gangs. The politicians urgently need outside help-and this should be aimed at strengthening their police forces and courts, rather than their armies, which should not be drawn into law enforcement.

But to students of the drug wars, pyrrhic victories that merely displace the problem of the drug barons to the next country are depressingly familiar. They are the story of the past three decades in Latin America. It is no wonder that a growing number of wise heads in the region have concluded that the drug war is costlier than legalising drugs. So have some brave souls in "consumer" countries (a distinction that has become blurred by rising drug consumption in Latin America and more synthetic drugs and cannabis cultivation in the United States, Canada and Europe). Sadly the converts tend not to include serving ministers.

An indefensible ban

The constraint on fresh thinking was on shameful display this week. A UN convention, reaffirmed in 2009, imposes a blanket prohibition on drugs. This includes even the traditional use of coca leaves (from which cocaine is extracted) by Andean Indians for chewing and tea. This ban has never been enforced and in 2009 Bolivia asked the UN to lift it-though not restrictions on coca cultivation for cocaine. With a deadline of the end of this month, America has lodged an objection and Britain looks poised to follow (see article). Traditional uses of coca are not addictive and are as much part of Andean culture as a cuppa is in Britain or beer in Texas. One reason for objecting seems to be that approval might open up a wider debate about legalising drugs. Yet the depressing news from Central America shows that this debate is long overdue.

Letters

On gun control, Italy, public-sector unions, London's bike-hire scheme, food prices, light bulbs, happiness

Jan 20th 2011 | from PRINT EDITION

Letters are welcomes via e-mail to letters@economist.com

A civil debate about guns



SIR - Contrary to the reasoning put forward in your reaction to the shooting in Tucson ("The blame game", January 15th), there is in fact no demonstrable connection between gun regulations and gun violence. Gun-related deaths in America have declined as the number of guns in private hands, and the permits to carry them in public, have increased. And, contradicting the predictions of gun-control advocates, the homicide rate in Washington, DC, has dropped since the Supreme Court struck down its handgun ban in 2008.

Furthermore, it is incorrect to think that "in no other decent country could any civilian...legally get his hands on a Glock semi-automatic." Most other "decent" countries do allow civilians to own semi-automatic pistols, with varying degrees of regulation, including France, Germany, Switzerland, Austria, Israel and Canada. International studies show no correlation between rates of gun ownership and homicide.

While a substantial majority of Americans support the right to keep and bear arms, reasonable people differ about the legitimacy and efficacy of gun regulations. But that disagreement should rest on facts, not superstition.

Clark Neily
Co-counsel for the plaintiffs in *DC v Heller*, heard at
the United States Supreme Court
Washington, DC

* SIR - As a member of the National Rifle Association for 30 years and holder of all their expert medals, I disagree with the notion that everyone is entitled to own any weapon, and I deplore the political power the NRA has bought. Honest citizens are entitled to own guns for hunting, target shooting or collection (without firing-pins), but mass killers are not.

And what good would it have done for Gabrielle Giffords to carry a gun? Not even Ed McGivern, a celebrated sharpshooter (who dented a quarter with his .38 as high in the air as I could toss it), would have survived that attack.

The assailant always has the advantage, and he is not going to give his victim the opportunity to use a weapon. Allowing more firepower onto the street just increases the chance of collateral damage.

James Reynolds
New York

* SIR - The events in Tucson were quite a tragedy. It is interesting to note, however, that a country 60 miles to the south has some of the strictest gun laws in the world. Does anyone feel safer in Mexico?

Brent Roberts
Scottsdale, Arizona

* SIR - Violent video games, Goth music and marijuana, all stewing Jared Loughner's brain? I expect better of you. Correlation is not causation.

Michael Blackwell
Buranda, Australia

* SIR - I respectfully disagree with your assertion that, "lax gun controls not vicious words are to blame" for the shooting in Tucson. A cursory perusal of the records will show that the cities in America with the most stringent gun-control laws, New York and Washington, have much more gun violence than does Arizona. As to the question of, "the nature of political discourse in the country", I am of the firm belief that there is an immediate and present need for us to bring civil discourse back into civic discussion.

I well remember when, both nationally and here in the Arizona legislature, the political tone was far more civil, and members of both parties were friends who treated each other cordially. In an effort to bring back that civility and collegiality, I have joined No Labels, an organisation committed to that end.

Bob Rosenberg
Phoenix

Italy wants you

SIR - Your article on Italy's brain drain was timely ("No Italian jobs", January 8th). Some of us in the Italian Parliament are acutely aware of the loss of young talent to our competitors, not to mention Italy's inability to attract young foreign graduates. That is why our Parliament, and not the Berlusconi government, acting in response to an initiative by Enrico Letta from the opposition Democratic Party, passed a bill with cross-party support to create fiscal incentives that make our country more attractive to skilled Italians and other European Union citizens.

This is the first in a series of initiatives designed to woo back expat Italians and eventually all-comers with talent to our shores.

Guglielmo Vaccaro, MP
Alessia Mosca, MP
Rome

The return of us and them

SIR - I thought your leader on public-sector unions was appalling ("The battle ahead", January 8th). You concentrated solely on demonising unions without one word as to why workers are so irate: the fact that their tax money has been used to bail out and prop up the banks that generated the financial crisis. Many workers are paying the price for that crisis by losing their jobs, homes and public services, while the people who caused it reward themselves grossly and obscenely.

T. Edwin
Heremence, Switzerland



SIR - If, as you insist, public-sector workers have been enjoying a "banquet" at taxpayers' expense, then how exactly would you describe the lavish feasts that those who operate in the financial industry have treated themselves to? "Wanton bacchanalia" might just about cover it.

Ken Scrudato
New York

* SIR - Pensions are like a bridge thrown over the river of old age. Every engineer will tell you that the bridge should not be wider than its capacity to support people or load. The same rule applies to pension funds. If a bridge collapses, should we condemn those who happened to be crossing it at the time? Should we not look for accountability from the architects, the building contractors and managers of the collapsed bridge?

Pensions are a contract between an employee and his employer that is not unlike the contract between a depositor and his banker. State workers that I know have paid up to 10% of their salaries over 35 years to benefit their pensions. The employers, private as well as public, kept the responsibility and the fees to manage the funds.

As for the viability of these funds, managers, with the collaboration of actuaries, accounting firms and bankers invested the funds in progressively more risky ventures in order to get higher yields to further reduce the participation of the employers to the pension funds. The fact is: they succeeded during the years of the bubble market and then they predictably failed. As a result of their mismanagement, the pension funds are undercapitalised. Where is their accountability?

Francois Lauzon
Retired airport fireman
Montreal

* SIR - I was a bit incensed to read that "in America teachers teach for a mere 180 days of the year" ("(Government) workers of the world unite!", January 8th). That statistic grossly under represents the huge amount of work that most teachers put in outside the school day (preparing class materials, marking papers, etc). Teachers make enourmous sacrifices for mediocre salaries.

David Jost
Goshen, Indiana

* SIR - Samuel Huntington pointed out the coming difficulties of the power of unions in a post-industrial world in a monograph published in *Comparative Politics*, January 1974. Huntington described the conditions that would be present in post-industrial societies and cause a conflict of interest between government employees and the larger population of American taxpayers, with elected officials caught in the middle. He explained that: "this conflict will place enormous strains on political leadership at all levels of government", which your article illustrates only too well.

Huntington went on to say, " it is not clear that any industrial or post-industrial society has resolved the problem of how to reconcile the freedom of public employees to organise and to strike, on the one hand, with the selection of public officials through competitive elections, on the other."

I think the issues surrounding the emerging crisis with public-sector unions that you highlighted are clearly on the mark.

Ken Szmed
Leavenworth, Kansas

* SIR - Margaret Thatcher's prophetic words have finally become reality: The trouble with socialism is that you eventually run out of other people's money.

Maurice Giraudier
Kailua Kona, Hawaii

Keeping in tandem

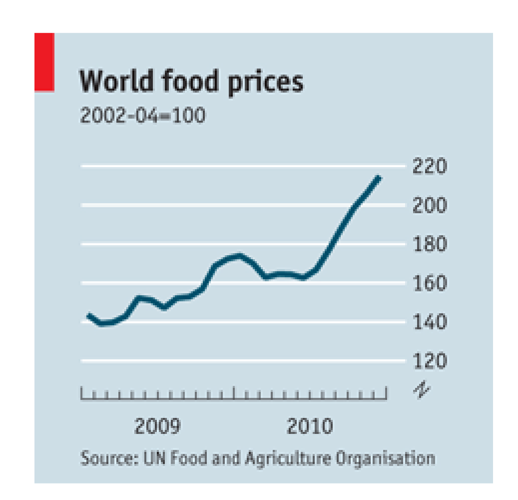
SIR - It was disappointing to read such a one-sided account of London's bicycle-hire scheme ("Grit in the gears", January 8th). Londoners have warmly embraced the mayor's scheme since its launch last summer. At the turn of the year nearly 110,000 people had signed up for membership and more than 2.1m journeys have now been made.

We were very clear that there would be teething problems with a scheme this size and the redistribution of the bikes has always been an important consideration. Serco, our contractor, monitors the patterns of usage to ensure the bikes are where they are needed. From a standing start, it has done well.

Based on tremendous public feedback as well as the findings in a recent scrutiny report by the London Assembly, the mayor and I believe that we have delivered a quality new mode of public transport that thousands of people can use and enjoy.

Kulveer Ranger
Adviser on transport to the Mayor of London

Rising food prices and nutrition



* SIR - Four items in your January 8th issue discussed the surge in food prices (The world this week, "Centeotl's pricier feast", "Inflated fears", "Enough to make your eyes water"). But there is another aspect to the impact of increases in staple food prices on the poor: a sharp rise in "hidden hunger", or deficiencies in essential vitamins and minerals. Poor households that have to spend an inordinate portion of their income on food respond to increased prices by first maintaining staples at the expense of more costly fruits, vegetables, meat, poultry and fish, which are all rich in life-saving vitamins and minerals.

Deficiencies in vitamin A, iron, zinc, and folic acid cause increased sickness and death and undermine human development and productivity. More than two billion people suffer from these conditions, which are exacerbated by increases in the price of staple foods.

We must ensure that vitamin and mineral supplementation programmes are reaching the very poorest, who are often left out of public-health programmes. We should also make it mandatory to fortify vitamins and minerals in food stuffs. Finally, we should encourage agricultural policies that promote food varieties selected for enhanced nutritional qualities, to produce a diverse variety of fruits, vegetables and small livestock.

Shawn Baker
Vice-president and regional director for Africa
Helen Keller International
Dakar, Senegal

Some bright ideas



* SIR - I would like to offer a different perspective on the fate of the incandescent bulb from that described in your lovely obituary (The World in 2011). The incandescent bulb is not dying; it is improving. Recent laws in the European Union, Australia, Canada and the United States do not ban any particular technology, rather they establish minimum efficiency requirements that today's beloved but inefficient incandescent lamps do not meet. These laws do not prevent the use of more efficient incandescent bulbs and have spurred the migration of improved incandescent technology from laboratories to shop shelves.

In Australia, where the import of inefficient lamps was banned in 2009, new types of incandescent bulbs account for a third of household light-bulb sales. Similar bulbs make up growing shares of European and American sales as well. To consumers, new incandescent bulbs look, feel, light up and dim down just like the old standbys; they still contain filaments, that, when heated, produce light.

The efficiency at which new incandescents produce light ranges from only slightly better than today's (becoming yesterday's) bulbs, up to twice as good; but they still use more electricity than the bulbs that have become a well-deserved symbol of energy consciousness, the spiral-shaped compact fluorescent lamp.

Nevertheless, in the case of the "death" of the incandescent bulb, Alfred, Lord Tennyson provides the right words: "Death's truer name is 'Onward'".

Laura Moorefield
Senior manager
Policy and research
Ecos
Durango, Colorado

Merry old souls

SIR - As you continue to explore the relationship of "happiness" with age, gender, personality and economics ("The U-bend of life", December 18th), you may want to return to the Greek and Roman philosophers from whom our use of that word with respect to peoples' lives originates.

Aristotle said that the purpose of acquiring "virtue" was to gain "*eudaimonia*". While that Greek word has often been translated into English as "happiness", it can be more accurately translated as "human flourishing" or "a well-lived life". Cicero, when dedicating his book "On Duties" to his son, wrote: "And what do I mean by a well-lived life, my son? I mean that you live a life that gives back to your country, gives back to your family, gives back to your fellow citizens."

That is almost certainly what America's Founding Fathers, who were students of Greek and Roman history and literature, used as guidance for their own lives and intended for others when they changed John Locke's "life, liberty and property" to "life, liberty and the pursuit of happiness".

Perhaps then there is another factor that makes people "happy", especially those who selflessly serve others in some way throughout their lives.

William Manthorpe
Rehoboth Beach, Delaware

SIR - Your article reminded me of the story of three men of faith answering the question, when does life begin? The Catholic priest replies that life begins at conception; the Calvinist parson says it starts at birth; the Jewish rabbi maintains that life commences when the children grow up and the dog dies. Although dog-lovers may abhor the last bit of that

proposition, the meaning is obvious: happiness is the release from the burden of responsibility. This may explain the U-bend.

Laszlo Jotischky
London

SIR - I found the U-bend argument riveting, not least because it corresponds almost exactly to my own experience at the age of 74. However, you omitted one factor: the ability to learn. One picks up tips from people through life and perhaps from books, while at the same time acquiring a knack of how to cope with a bad mood or a rainy day.

One discovers activities, such as music, dancing or meditation, which are conducive to happiness. Hence, the more experience you have, and so roughly speaking the older you are, the "better" you become "at it". As the Latin poet Horace put it, remember to keep cool in bad times and don't get above yourself when things go well.

Antony Black
Dundee



The boy without the thorn in his side

SIR - Some of your assertions appeared to be at odds with the experiences of my generation. In 1984 a 25-year-old songsmith from near Salford penned "Heaven Knows I'm Miserable Now". Now at the age of 51, close to the nadir of your happiness graph, Mr Morrissey is quite perky by all accounts. It seems that by securing a sizeable chunk of change and relocating from Manchester to California, you can indeed buck the trend.

Jake Turnbull
Newcastle upon Tyne

* Letter appears online only

Index | Briefing

Tunisia

Ali Baba gone, but what about the 40 thieves?

Jan 20th 2011 | *TUNIS* | from PRINT EDITION

The flight of Tunisia's longtime president leaves the small country he ruled and robbed in upheaval. Its Arab neighbours wonder whether it's the start of a trend



"TUNISIA now lives in fear," Libya's ruler, Muammar Qaddafi, told his people. "Families could be raided and slaughtered in their bedrooms and the citizens in the street killed as if it was the Bolshevik or the American revolution."

Others seem less sure what caused Tunisia's upheaval, where it will go or even what to call it. Some have labelled it the jasmine revolution. Close at hand, however, the continuing unrest in Tunisia, for long the most politically neutered of Arab countries, does not bring to mind the sweet-smelling flowers that men here tuck jauntily behind an ear. What's happening reeks more of sweat, tear gas and burning rubber, and has brought Tunisians as much anguish as pride or pleasure.

It cannot quite be termed a revolution, at least yet. The main instruments of control for the past 50 years, the police and the ever-ruling RCD party (a French abbreviation of Constitutional Democratic Rally) are battered and wobbly but still standing. They face no strong, cohesive opposition, no charismatic leader waiting in the wings, armed with a mission or an ideology. Yet with 78 civilians dead by official count and with street protests continuing into a sixth week, it is certainly bigger than a revolt.

Everyone knows what started it: the self-immolation on December 17th of a despairing, jobless youth named Muhammad Bouazizi in the main square of Sidi Bouzid, a town in Tunisia's hardscrabble interior. Yet there is a fierce dispute about what has sustained the revolt, encouraging furious protesters to the streets of prosperous coastal cities, galvanising near-moribund trade unions and opposition groups into action, and bringing about the dramatic scuttle into exile on January 14th of Zine el-Abidine Ben Ali, president for the past 23 years. And nobody is sure what Tunisia's troubles will lead to: a transition to multiparty democracy, a military coup or a prolonged period of turmoil.

What is sure is that the Tunisian uprising has not only put an end to one of the more insidiously oppressive and comically rapacious strongman regimes in a region inured to them. It has also put Mr Ben Ali's fellow rulers-for-life on notice that they, too, may suddenly find themselves without friends or a country. Mr Bouazizi's public suicide has spread a grisly rash of copycat self-torchings across north Africa, from Mauritania to Egypt. Their acts of self-sacrifice hope to incite a spiral of events similar to Tunisia's.

Perhaps they will. Given the extreme social stresses shared by many Arab societies, and particularly the anger of soaring numbers of jobless, jeans-clad youths against the ageing cynics in suits and uniforms that have for so long denied them a role or a voice, it is not too far-fetched to conjure a sweeping wave of change, much as in Europe in 1989.

Yet Tunisia's circumstances are in some respects unique. With a population that is ethnically and religiously homogenous, recognised borders that are centuries old, and a tradition of centralised government that predates colonisation by France in 1881, Tunisia has more solid foundations than many Arab states. Despite the country's paucity of natural resources, its 10.6m people enjoy relatively good standards of health, education and other public services. It has a high level of home ownership and reasonably solid national accounts. Its economy, integrated with the outside world as a magnet for investment in manufacturing, offshore services and tourism, has grown at an annual average of 5% for the past two decades.

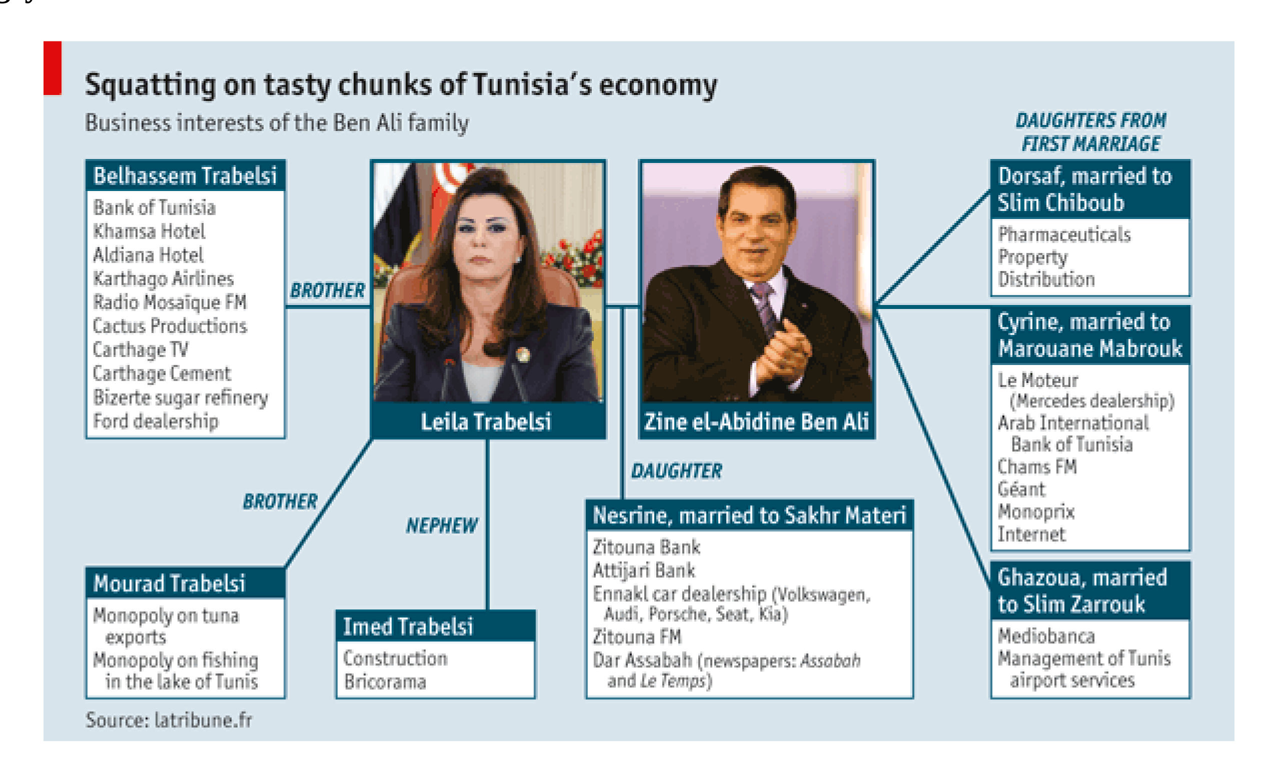
That modest record of success, contrasting starkly with the messy dysfunction of Algeria and Libya, the oil-rich countries Tunisia is squeezed between, goes a long way to explaining why Tunisians have put up with their stifling political order. Mr Ben Ali did not invent this system. His predecessor, Habib Bourguiba, a passionately Francophone lawyer who led Tunisia to independence in 1956, created a paternalistic, monopolistic ruling party and a cult of personality during three decades of rule. Like Turkey's Kemal Ataturk, Mr Bourguiba tried single-handedly to yank his country out of old ways, championing women's rights and enforcing strict secularism.

When Mr Ben Ali, newly installed as interior minister, ousted the ageing but respected president in a palace coup in 1987, he was greeted as a needed breath of fresh air. Secularists and even liberals at first applauded his hounding of the Ennahda party, a mild Islamist movement, linked to the Muslim Brotherhood, that had flowered in the chaotic waning years of Mr Bourguiba's rule. On largely spurious charges of terrorism its leaders were either jailed or forced into exile, and the movement essentially eradicated.

Sadly, rather than subsequently broadening freedoms, the ex-policeman crushed them, infiltrating watchful RCD party hacks into trade unions, university faculties and other once-independent institutions. Benalisme, as Tunisians sometimes dubbed his style of rule, brought with it increasingly farcical elections, an absurdly adulatory press and dread of the pervasive, petty and vindictive security services. During Algeria's bloody civil strife in the 1990s, Tunisians joked of a plump, sleek Tunisian dog fleeing across the border and meeting a ragged, starving Algerian one. "What on earth are you doing here?" asked the Algerian dog. "I came here to bark," was the forlorn reply.

Tunisia came to have more police than France, a country with six times more people. With few real threats to the state to combat, Mr Ben Ali's bloated security service specialised in such tactics as planting evidence in order to blackmail suspects. Taxi drivers commonly sought protection by joining the RCD or working as police informants. "Going too often to the mosque could mean a summons to State Security," says one. "They could lift your licence, and put you through hell to get it back."

Those hungry relatives



Benalisme also brought corruption, particularly at the level of the president's own family. With time the web of influence extended both to the husbands of Mr Ben Ali's four adult daughters and to the many relatives of his second wife, Leila Trabelsi, a former hairdresser whom he married in 1992. Between them, the Trabelsis and Mr Ben Ali's sons-in-law came to control a huge slice of the economy (see diagram). In recent years their tentacles penetrated deep into Tunisia's financial system, extracting sweetheart loans from once-respectable banks.

For a society that remains mostly poor or tenuously middle class it was not the possession of big assets that rankled so much as the flaunting of baubles, such as the flashy cars and villas in Tunisia's most exclusive districts. What grated most with Tunisia's small elite was the upstart first family's habit of elbowing out competitors and flaunting of power. Giving a cut to one of the favoured circle came to be seen as *de rigueur* in order to gain a licence or agency quickly. "Of course I brought in a Trabelsi, without his even asking," a Tunisian economist recalls a business acquaintance declaring defensively. "Its just a tax, so I don't have to pay other taxes."

Mr Ben Ali himself feigned ignorance of such things despite the rising smell, and the rising cost to the country of such shenanigans. An American diplomatic cable from 2008, revealed in early December by WikiLeaks, described the ruling family as the nexus of corruption and a quasi-mafia. Tunisian investors wary of getting caught in this web preferred to forgo business ventures and instead bought property or stashed funds abroad, continued the cable, so dampening growth and helping to sustain high unemployment.

A report this month by Global Financial Integrity, a watchdog group, corroborates this assessment. "The amount of illegal money lost from Tunisia due to corruption, bribery, kickbacks, trade mispricing and criminal activity between 2000 and 2008 was, on average, over $1 billion a year," it estimates. That is a substantial sum for a country whose GNP barely reaches $80 billion at purchasing-power parity.

The sprouting of fancy shopping centres, yacht marinas and housing developments along Tunisia's breezy coast provided a shiny veneer of prosperity. Even bleak provincial towns and the slums around prosperous cities look tidy by the standards of other developing countries. But the exterior sheen conceals a growing sense of anomie, compounded by swelling unemployment and material expectations fed by rising educational standards.

Ezzeddine Larbi, a former World Bank economist who left the country to live abroad, found that unflattering economic statistics were routinely suppressed or massaged. He reckons that unemployment, officially put at 14%, is closer to 20% for university graduates, and 27% overall for the 20-29 age group. Such numbers are not unusual for the region, but other factors exacerbate the problem in Tunisia. Its economic model, based on undercutting European labour costs, means that many of the jobs on offer are unskilled and unrewarding. University graduates do not aspire to be waiters, call-centre operators or garment stitchers. At the same time, Tunisia's tidiness and success at building a middle class mean that a black economy cannot absorb legions of street vendors and house servants, as in Egypt and Morocco.

This partly explains why Mr Bouazizi poured petrol on himself. A university graduate, he had tried to scrape a living selling vegetables from a stall which was confiscated by the police. When a few young men rioted in protest at his action, poorly trained policemen responded violently. Protests spread to nearby towns, and several youths were killed by police gunfire, further raising public anger.

Mr Ben Ali was not insensitive to the brewing trouble. He visited Mr Bouazizi in the hospital where he lay dying, offered compensation to his family and sacked the provincial governor as well as a government minister. The unrest might have petered out but for an unexplained escalation. On January 8th the toll of deaths from police gunfire suddenly surged, from fewer than ten to more than 30.

Many assumed an order had been given to stamp out the unrest with terror. The fury spread to Tunisia's coastal cities, growing as gory imagery relayed by cell phones and the internet clashed with the sanitised blandness of state television. Actors that had previously stayed on the sidelines, such as student groups, the remaining, puny opposition parties and the once-powerful trade-unions organisation, joined the fray. But the focus had changed: people were calling for Mr Ben Ali's head.

In a rambling television address, the president blamed foreign agitators for the troubles. Sacking his feared interior minister, he promised a huge jobs programme, and inquiries into corruption and excessive police force. But this was too little, too late-and it also showed weakness. Rioters were now fighting the police in pitched battles, torching police stations and sacking banks and shops, particularly those thought to belong to RCD members.

In some cases the police themselves were accused of looting, either as part of a plan to tarnish the protesters and frighten the middle class, or simply to profit from the collapse of order. So tarnished was the reputation of the police that Mr Ben Ali belatedly asked Tunisia's army to intervene. Some units did enter the capital, but refused to use force against protesters, who greeted them with cheers.

Still, few Tunisians expected the president to go, even when as many as 40,000 people gathered on January 14th at the headquarters of the Interior Ministry on Tunis's stately Avenue Bourguiba, braving torrents of tear gas and live fire. That evening, with a curfew in place and army tanks sealing Tunis's main airport, Mr Ben Ali and his immediate family slipped out of the country on an aircraft that eventually, having been rebuffed by France, took them to Saudi Arabia. "What an irony that a guy who banned veils should end up with the Wahhabis," was the Twitter comment of one Tunisian writer.

The following day witnessed a near-complete breakdown of order, with the once ubiquitous police vanishing from streets across the country. Near the port of La Goulette on Tunis's outskirts, youths raided a lot filled with cars imported by Mr Ben Ali's son-in-law, Sakhr Materi. Surrounding streets were soon filled with flaming, overturned Porsches, Volkswagens and Kias. In the coastal resort of Hammamet, looters trashed Mr Materi's villa and slaughtered his pet tiger.

More disturbingly, reports emerged of attacks by suspected saboteurs and snipers, with gun battles erupting in the capital. Many Tunisians assumed the culprits to be members of shadowy, rearguard units loyal to the ousted president. Amid a swirl of rumour, some detect a plan to foment chaos and so pave the way for Mr Ben Ali's return as the restorer of order, perhaps backed by his friend Colonel Qaddafi. Frightened by such talk, groups of civilians across the capital have set up voluntary guard units, manning checkpoints and searching cars for weapons. Special army and police units are also said to have arrested suspected saboteurs.

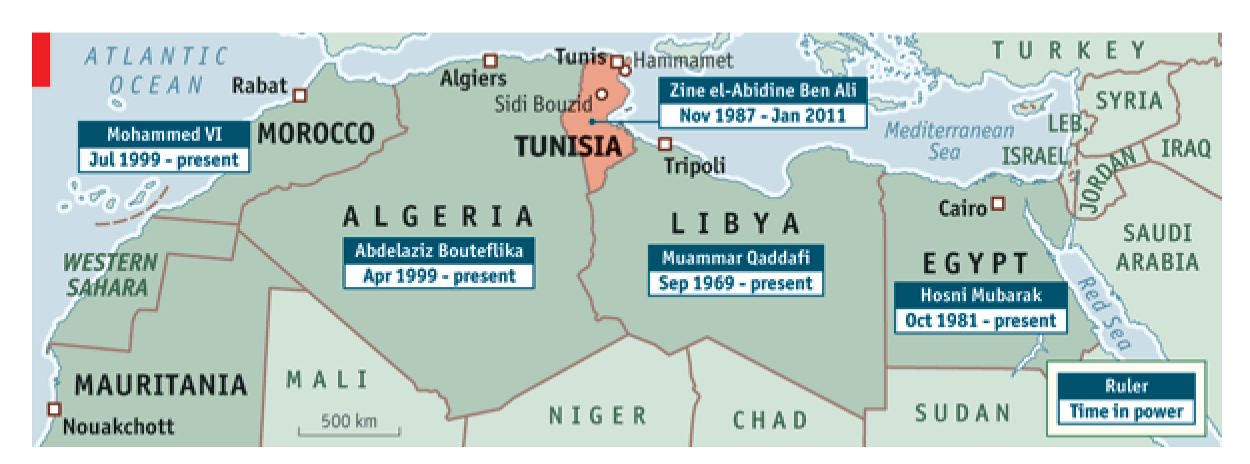
As a result, by January 19th a measure of calm had returned to Tunis, with many shops and businesses reopening, and no sound of gunfire during the (now shorter) nightly curfew. Elsewhere, there were no reports of violent unrest or looting, except for vandalism against some local RCD offices, indicating that the party has emerged as a new focus of pressure.

The political situation remains foggy. After Mr Ben Ali's departure, his prime minister since 1999, Mohammed Ghannouchi, a veteran RCD leader, announced he would form a government of national unity, with the speaker of parliament, Foued Mebazaa, temporarily filling the presidency. Seeking to assuage public anger, Mr Ghannouchi announced the lifting of all censorship, the institution of three independent commissions to investigate corruption, human-rights abuses and political reform, the release of all political prisoners and preparations to hold free elections within six months.

The new cabinet he announced included several opposition figures, but kept the main ministries for RCD members. Before the new cabinet could meet, four of its ministers had resigned in protest at lingering RCD influence. It is not yet clear whether palliatory measures by the party, which has expelled Mr Ben Ali and senior cronies, and accepted the resignation of Mr Ghannouchi and Mr Mebazaa, were enough to lure the ministers back.

The Tunisian public appears divided in response. Many among the educated middle class would prefer to give the new government a chance, fearing a slide towards military rule, or worse. But smaller demonstrations continue across the country calling for the sacking of all RCD ministers and the inclusion of exiled opposition leaders. In any event, patching up the political system will not be easy. With a constitution tailored to bolster Mr Ben Ali, a sitting parliament packed by the RCD, and institutions such as the police and courts deeply compromised, the mechanism for the kinds of sweeping change demanded by many Tunisians is not there.

Opposition forces, fractured by years of repression and manipulation, are not much help, and lack figures with popular authority. The potential role of Islamists, so far markedly muted, remains an unknown. For the time being the shadowy supporters of the banned Ennahda party are backing the provisional government, for fear of a military takeover that could see their hoped-for revival further postponed. Their leader, 69-year-old Rashid Ghannouchi, remains in exile in London, awaiting an amnesty since he formally faces a sentence of life in prison.



Repercussions in the wider Arab world hinge on the outcome in Tunisia. Signs of unrest have already emerged in Egypt, Algeria, Jordan, Yemen, Libya and Sudan. "The Tunisian model is very similar to its Egyptian counterpart, and the extremely happy response to events there on Egyptian streets shows that Egypt might witness solutions like the Tunisian one soon," noted Ayman Nour, an Egyptian politician who was thrown in jail after challenging Hosni Mubarak in an election in 2005.

Governments have also taken note, intervening recently to keep down the rising cost of basic staples in several countries, and showing unwonted compassion for the unemployed. But some, such as Colonel Qaddafi, have drawn opposite conclusions, and may prove more determined to face down pressures than Mr Ben Ali was.

Many of the region's countries look, on the surface, to be far more fragile than Tunisia, with equal volumes of anger and far deeper social woes. But different factors serve to bolster even unpopular governments. In Syria the ever-present danger

of war with Israel mutes dissent. The Egyptian state, despite its appalling record in running other things, wields a large force of riot police that is well equipped, highly trained and very experienced, and so less likely to provoke outrage by excessive violence. Egypt also has a relatively free press. This not only gives healthy air to protest, but acts as the sort of early-warning system that Mr Ben Ali, due to his own repressive tactics, sorely lacked.

There is another way in which Tunisia's experience could prove subtly inspiring. "The one constant in revolutions is the primordial role played by the army," said Jean Tulard, a French historian of revolutions, in an interview in *Le Monde*. So far Tunisia's army, kept small to forestall coup attempts, has won kudos for holding the fort, and not playing politics. Yet it is the army which is believed to have persuaded Mr Ben Ali to leave. Perhaps a few generals elsewhere in the Arab world are thinking that they, too, might better serve their countries by doing something similar.

Index | United States

Regulation and the Obama administration

Red tape rising

Jan 20th 2011 | *WASHINGTON, DC* | from PRINT EDITION

The regulatory state is expanding sharply. But Barack Obama hints that there may be moderation ahead

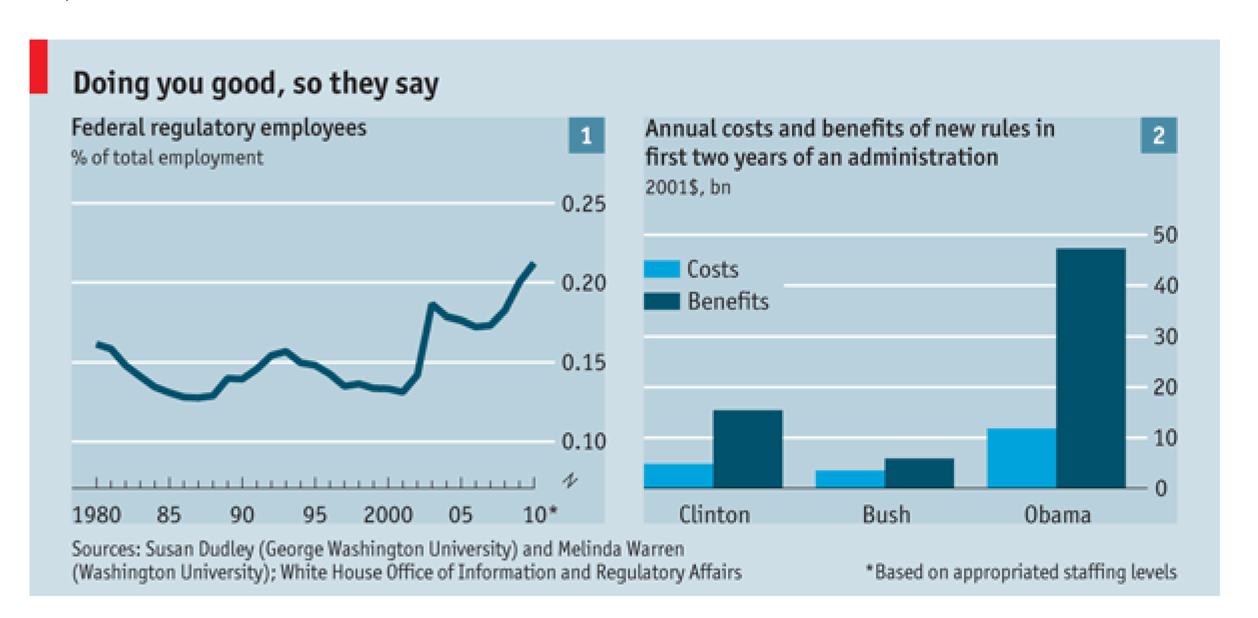


EVER since his thumping in the mid-term elections, Barack Obama has been busily mending relations with business folk. He has extended existing tax cuts, introduced new ones, completed a free-trade deal and appointed a banker as chief of staff. Now he is attending to their biggest grievance: that he has enmeshed them in stifling new rules, from health care and finance to oil-drilling and greenhouse gases.

Unlike many charges lobbed at Mr Obama, this one is well grounded. In his first two years in office the federal government issued 132 "economically significant" rules, according to Susan Dudley of George Washington University. ("Economically significant" means that either the rule's costs, or its benefits, exceed $100m a year.) That is about 40% more than the annual rate under both George Bush junior and Bill Clinton. Many rules associated with the newly passed health-care and financial-reform laws are still to come.

Existing rules are also being enforced more keenly. The workplace-safety regulator slapped employers with 167% more violations in Mr Obama's first year than in Mr Bush's last, according to OMB Watch, a liberal watchdog. The Food and Drug Administration (FDA) has stepped up scrutiny of drugs that have already been approved for sale. Last year it barred the use of Avastin for breast cancer, not because it was unsafe but because its benefits seemed too uncertain. The

regulatory workforce has grown 16% in Mr Obama's first two years in office, to 276,429, while private employment has fallen (see chart 1).



Has this extra regulation made the economy worse off? Not necessarily. The White House Office of Information and Regulatory Affairs (OIRA), which vets most new federal rules, reckons that although Mr Obama's regulations cost more than his predecessors', they also bring greater benefits (see chart 2): fewer lives lost from inhaling mercury, being hit by lorries, or eating contaminated food. "I take any costs seriously, but they may be worth incurring if, in return, we get much higher benefits," says Cass Sunstein, who heads OIRA and, like Mr Obama, taught law at the University of Chicago.

Even business concedes that some new rules were long overdue. A law passed last December gives the FDA sweeping new authority to order food recalls, track the supply chain for fresh food and order companies to submit food-safety plans, while authorising some 1,000 new staff to carry out its orders. Despite its intrusiveness, food manufacturers backed the law in the hope that it would restore public trust in the food system, which had been shaken by fatal outbreaks of *E. coli* and salmonella.

Nonetheless, Mr Obama now seems more sympathetic to business complaints about regulatory overkill. On January 18th he signed an executive order laying out his philosophy of regulation. It reiterates guidelines first issued by Mr Clinton and adhered to by Mr Bush: rules should be subject to cost-benefit analyses, imposed in the least costly way and leave companies free to work out how to comply. Mr Obama also went further, ordering all regulatory agencies to put in place within 120 days a system for reviewing old rules to see if they can be amended or repealed, and to ease the burden of regulation on small businesses.

Yet the order also expands the scope of regulation by telling agencies that they may consider "values that are difficult or impossible to quantify, including equity, human dignity, fairness, and distributive impacts". That is an important consideration for rules such as better access to toilets for the disabled. The risk is that such criteria could be used to justify rules that cost the earth. Banning limits on health insurance, for example, as the health-care law does, may reduce the anxiety of people who might otherwise lose coverage, but whether that is worth the increase in premiums is impossible to say.

A similar attitude underlies both the thicket of homeland-security rules that has sprung up since the terrorist attacks of September 2001, and financial reforms since the banking crisis. These are justified largely by arguing that another terrorist attack or financial crisis would be unimaginably damaging. But since the probability of either event seems unknowable, so are the benefits that might accrue from the laws. Vikram Pandit, the chief of Citigroup, has likened the new Basel capital rules to maintaining a standing army large enough to fight the second world war.

Also unquantifiable is the innovation that may be deterred by regulation. Michael Mandel, a scholar at the Progressive Policy Institute, a think-tank, says some of Mr Obama's rules, though well intentioned, interfere with the most dynamic parts of the economy. Rules meant to deter the abuse of student aid by for-profit colleges could stunt the growth of college courses taught over the internet; tighter conditions on drug approvals, prompted by much-publicised scandals, raise the cost of drug research, especially for small companies; and "net neutrality" rules could expose internet-access providers to stifling litigation.

Mr Obama's regulatory surge would be less damaging if it had not followed one by Mr Bush, Mr Mandel says. Because of fears about national security, telecoms and internet companies came under pressure to accommodate federal

eavesdroppers. The Sarbanes-Oxley accounting law has made it more expensive for start-up companies to list their stock publicly.

Perhaps Mr Obama's new edict will hack away some of the regulatory undergrowth that has flourished over the decades. But business could be waiting a while for results. In December the Environmental Protection Agency took saccharine, an artificial sweetener, off its list of hazardous materials-more than a decade after scientists had concluded it was not carcinogenic after all. Mr Sunstein vows: "It isn't going to take ten years to get rid of rules that deserve to be got rid of."

Index | United States

Defining poverty

Measure by measure

Jan 20th 2011 | *CHICAGO* | from PRINT EDITION

The world's richest country tries to count its poor

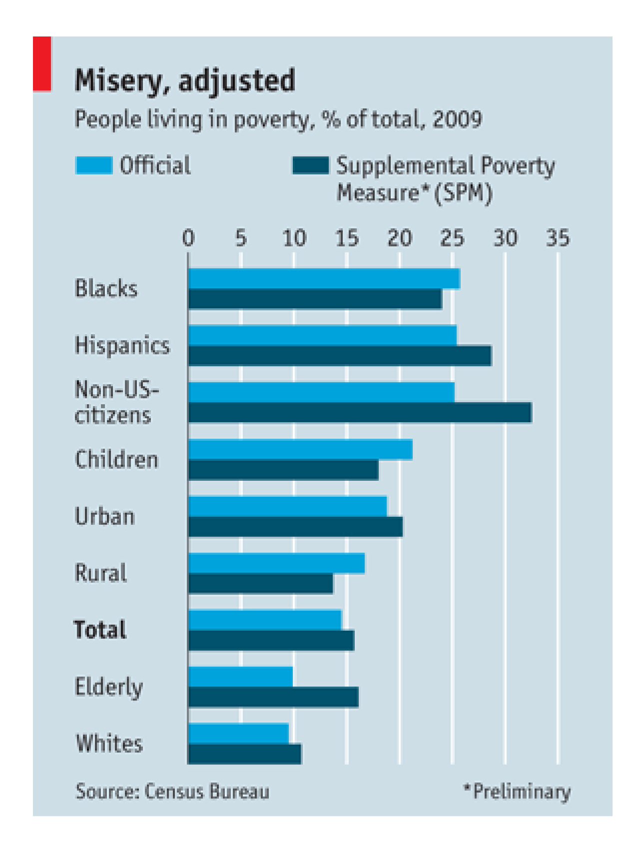


MOST people have an inherent sense of what it means to be poor. But choosing a definition is much trickier. Is poverty an absolute or relative condition? What is a decent standard of living? Such questions have dogged America's social scientists for decades. This month the Census Bureau published a preliminary estimate of poverty, using a new definition. It was 16 years in the making. But it is not quite finished yet.

Poverty means different things in different countries. In Europe, the poor are those whose income falls below 60% of the median. Britain uses three measures: one relative, one absolute and a broader indicator of material deprivation, such as whether a child can celebrate his birthday. The concept of poverty becomes even more slippery when attempting international comparisons. The United Nations' "human- development index" assesses countries across a range of indicators, such as schooling and life expectancy.

America's official poverty measure is far simpler. Developed in the 1960s, the poverty threshold represents the basic cost of food for a household, multiplied by three. A family is judged to be poor if its pre-tax income falls below this threshold. But the official measure provides only a blurry picture. Food spending has become a flimsy reference point-in 2009 groceries accounted for just 7.8% of Americans' spending. The poverty indicator does not account for programmes that help the poor, such as the earned-income tax credit, nor does it adjust for regional variations in the cost of living. In 1995 the National Academy of Sciences recommended changing the measure, but only now is a new one close to being established.

The "supplemental poverty measure" (SPM) will not replace the official one, which is used to determine eligibility for government programmes. Rather, census officials hope the new indicator will provide a better understanding of America's poor, by measuring both the needs of families and the effect of government help. The SPM estimates the cost of food, clothing, shelter and utilities, then adds a further 20% for other expenses. This threshold is adjusted for the cost of living in different regions and for whether a family owns or rents its home. To assess a household's ability to pay for basic expenses, the SPM counts cash income as well as food stamps, tax credits and other government support, minus tax payments, work expenses and out-of-pocket medical costs.



Final figures are due to be published in the autumn, but preliminary results were released this month. In 2009 15.7% of Americans were poor, compared with 14.5% in the official measure (see chart). The share of those in extreme poverty fell, relative to the official measure, thanks to the inclusion of government support. The poverty rate dropped in rural areas and rose in urban and suburban ones. It jumped in the north-east and the West, while staying almost level in the South and falling in the Midwest. The most dramatic rise was for the elderly-from 9.9% in the official measure to 16.1% in the SPM, in part because of their high medical expenses.

Timothy Smeeding of the University of Wisconsin, long a critic of the old measure, says that the SPM is a massive improvement. Some conservatives, however, are horrified. Most objectionable, according to Robert Rector of the Heritage Foundation, is that the new measure pegs household expenses at the 33rd percentile of American spending. This, he argues, makes the SPM a relative measure, rather than an absolute one. "It measures inequality," Mr Rector insists, adding that it will help advance a misguided anti-poverty agenda.

For all the time spent developing the SPM, it is still a work in progress. Though first official numbers are supposed to be published in the autumn, even this is uncertain. Surveys must be expanded to collect additional data. The project needs about $7.5m, and a newly conservative Congress may be reluctant to provide it.

Index | United States

Filibuster reform

Talking cure

Jan 20th 2011 | *WASHINGTON, DC* | from PRINT EDITION

Frustrated Democrats try to get around the Senate's rules about changing the rules

THE first known use of the filibuster, meaning an attempt to prevent the passage of a law by time-wasting, was in ancient Rome, where Cato the Younger sometimes stalled votes in the Senate by blathering on all day. At first, the filibuster helped him to thwart the ambitions of Julius Caesar. But Caesar eventually trumped him. Next week a few Democratic Caesars in America's Senate are hoping history will repeat itself.

A torrent of words

Famous filibusters of American history

Who	When	Why	Notable facts
John Calhoun	1841	Against establishment of a national bank	Considered the first modern filibuster
Robert La Follette	1908	Against a banking bill that would have allowed the issue of currency backed by any securities	Spoke for over 18 hours, sustaining himself on eggnog, which he complained had been drugged. Analysis showed that it contained a deadly dose of ptomai
Robert La Follette and others	1917	Against a bill to arm merchant ships against German submarines, for fear it would pull America into WWI	Debate turned violent. La Follette tried to throw a brass spittoon at the presiding officer. Resulted in introduction of the cloture rule
Huey Long	1935	To require Senate confirmation of the National Recovery Administration's senior employees	Read and analysed the constitution; gave recipes for fried oysters and potlikk Spoke for 15 hours 30 minutes. A bathroom break forced his departure from t
Wayne Morse	1953	Against Tidelands Oil legislation	Spoke for (a then record) 22 hours 26 minutes
Strom Thurmond	1957	Against the Civil Rights Act	Spoke for (a still record) 24 hours 18 minutes. Prepared by spending time in t Senate steam room to dehydrate. Brought his lunch and read from the phone
Robert Byrd	1964	Against the Civil Rights Act	Spoke for 14 hours 13 minutes
Robert Griffin and others	1968	Against promotion of Justice Abe Fortas to Chief Justice of the Supreme Court	First filibuster against a Supreme Court nominee. One senator read political m

Source: *The Economist*

American senators have resorted to filibusters now and again for 170 years (click left for table). Indeed, the practice has been formalised: Senate rule number 22 states that a filibuster can be overridden only by a vote of 60 of the 100 senators. But the manoeuvre, once rare, has become commonplace. Senate Democrats complain that there have been more filibusters since they took control of the chamber four years ago than in the 60 years from 1920 to 1980.

That, they continue, has stymied many bills that enjoyed majority support, and caused others, such as Barack Obama's health-care reforms, to be watered down to meet the higher threshold. Worse, for several decades now, recalcitrant senators have not even been required to go to the trouble of harping on for hours on end: they can merely signal their intent to filibuster, with no inconvenience. Last month, before the new Congress convened, all the returning Democratic senators wrote to Harry Reid, their leader, calling on him to push through a reform.

But changing the rules is even harder than overcoming a filibuster: it requires the approval of 67 senators. That is beyond the reach of the Democrats, with their slender majority of 53. So three of them-Tom Harkin of Iowa, Jeff Merkley of Oregon and Tom Udall of New Mexico-are proposing a procedural gimmick to get around the rules. This hinges on an arcane debate about whether the Senate is a "continuing body", always working under the same rules, or an intermittent assembly which is simply assumed to have adopted the rules prevailing in the previous Congress unless someone objects. That second, more informal theory, the trio note, seems more in keeping with the constitution.

Their resolution to change the rules, put forward earlier this month, could, they contend, be approved by a simple majority vote. It would leave intact the 60-vote threshold for breaking filibusters, but restore the requirement that filibustering senators actually take to the floor and talk until the majority gives up. The Senate is due to consider the measure next week.

The Republicans, predictably, are up in arms. They argue that the filibuster, although not mentioned in the constitution, is in keeping with the Founding Fathers' intention that the Senate should be a more thoughtful, conservative body than the House of Representatives. They have only resorted to the filibuster so often, they add, because the Democrats have prevented them from offering amendments to the bills in question (although the Democratic trio's proposal would guarantee them at least three amendments on every bill). Moreover, they argue, the Democrats would be opening a can of worms by changing the rules with a simple majority: if the Republicans gain the upper hand at the next election, they would feel no compunction about doing the same.

A few Democrats are hesitating. Some see the whole proposal as a negotiating tactic, to encourage the Republicans to embrace milder reforms or at least use the filibuster more sparingly. Since the Democrats have lost control of the House, and will therefore need to compromise with Republicans on all legislation anyway, winning firmer control of the Senate

would do them little good. But then again, striving mightily to fix "broken" Washington always goes down well with voters.

Haley Barbour's ambitions

Inside man

Jan 20th 2011 | *KEMPER COUNTY, MISSISSIPPI* | from PRINT EDITION

How might Mississippi's governor play on the national stage?



Not cut out for tea parties

LAST December, in a canvas tent erected on a building site in rural east Mississippi, Haley Barbour worked the dirt-floored space as deftly as Sonny Rollins on a saxophone. He had come to Kemper County to break ground for a coal-fired gasification plant designed to capture, store and eventually sell most of its emissions. "As long as I'm governor," he told the crowd, "Mississippi will have an energy policy, and that policy is more energy." The line, bluff, direct and vintage Barbour, drew cheers.

But Mr Barbour will not be governor much longer. He is in the last year of his second term, and cannot run again. Speculation is mounting that he will run for president, though Mr Barbour says he will make no decision until Mississippi's legislative session ends in April. Certainly, if he harbours any presidential ambition, this is the time to follow it. By 2016 he will be 68 and five years out of office. Whether he can win is a trickier question.

If he fails it will not be for lack of political skills. After an unsuccessful Senate bid in 1982 he decamped to Washington, where he worked in Ronald Reagan's White House (his boss there was Mitch Daniels, now governor of Indiana and another potential presidential candidate in 2012), and on George Bush senior's campaign. He headed the Republican National Committee from 1993 to 1997, during which time his party took control of the House of Representatives for the first time in 42 years. He jointly founded a lobbying firm and turned it into a Washington powerhouse. He is a formidable fund-raiser. As head of the Republican Governors Association during the 2010 elections he funnelled over $100m to races around the country, helping Republicans win 23 of the 37 governors' mansions in play, including 11 previously occupied by Democrats.

Marty Wiseman, who heads the Stennis Institute of Government at Mississippi State University, says that no one is a more knowledgeable or effective political strategist than Mr Barbour. Important as those skills are to party insiders, however, to voters they could be a liability, particularly if tea-partiers play as big a role in the 2012 cycle as they did in 2010. Painting him as a creature of Washington will be easy.

Mr Barbour's lobbying career is similarly double-edged. On the one hand, he vaunts his success: "Lobbying is advocacy, and advocacy is a huge part of a president's job. I understand it." And indeed his Washington experience and abilities as an advocate served him well in the immediate aftermath of Hurricane Katrina, which left 100,000 Mississippians homeless: Mississippi received over $24 billion in federal funds. He has also directed a number of big manufacturing concerns to Mississippi, including the Kemper County coal plant, which is expected to create 260 permanent jobs and 1,000 during peak construction, and a Toyota factory in the state's rural north that will employ 2,000 people.

On the other hand, Mr Barbour's argument sounds far better on paper than it will in the heat of a campaign. Opponents will no doubt bring up his work on behalf of tobacco companies and ask, as others have, whether it impelled him to kill a statewide anti-smoking programme in 2006 and to twice veto a bill that would have replaced the state's grocery tax with a higher tax on tobacco. And for all his economic development, Mississippi still has the lowest income per head of any state in the union, as it did when he took office.

And then there is his propensity to make racially insensitive comments. The *New York Times* reported in 1982 that Mr Barbour had warned an aide who used racial slurs to stop, lest he be "reincarnated as a watermelon and placed at the mercy of blacks." More recently he praised the Citizens Council, a segregationist group, for keeping the peace in his town when he was growing up, though he retracted later.

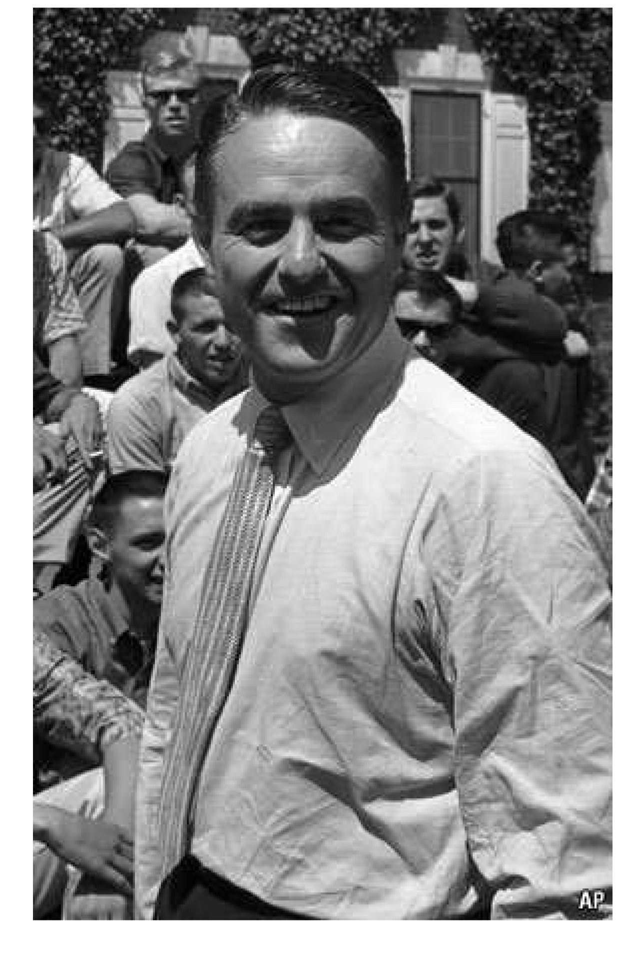
It is hard to see many northern, black or other minority voters backing a candidate given to such remarks, especially when the alternative is Mr Obama. Sometimes the best place for a gifted behind-the-scenes strategist is behind the scenes.

Index | United States

Sargent Shriver's passing

Altruism personified

Jan 20th 2011 | from PRINT EDITION



Civility, altruism, public service, all publicly pined for since the Tucson shootings, seemed summed up in Sargent Shriver, who died on January 18th. In a world split between heavily armed East and West, Mr Shriver's Peace Corps, set up in 1961 under his direction, sent students abroad to foster friendship and be useful. In America itself, riven by race and Vietnam, he led programmes-Head Start, VISTA, Community Action-that looked beyond colour and ideology to improve the lives and chances of ordinary people. And not least, Mr Shriver regularly put his own ambitions aside to help his thrusting in-laws, the Kennedys, grab and hold on to power. Too idealistic for the political rat-run, perhaps; too naive to be president, even if he had wanted it and voters had wanted him; just too darn nice, it seems, ever to have flourished in the present climate. But by no means ineffective, for all that.

Index | United States

The cotton industry

Bloom times

Jan 20th 2011 | *CORPUS CHRISTI, TEXAS* | from PRINT EDITION

The best prices since the civil war



White stuff, Texas-style

LIFE in the modern American cotton industry is relatively calm. In recent years, for example, producers began using plastic straps to secure bales of ginned cotton to the trucks. Plastic bands are safer than steel, and recyclable. So the events of 2010 took some people by surprise. John Barrett, a cotton producer based in south Texas, explains that around March of last year most of the farmers he works with were happy to contract for that year's crop at roughly 80 cents a pound. It was, historically speaking, a good price. Hardly anyone expected that, by harvest time, prices would have nearly doubled. In December cotton futures hit a nominal record of $1.59 a pound. The last time prices were so high was during the civil war and its aftermath.

This time round, circumstances are less dramatic. The demand for new clothes is growing as the world pulls out of recession and as incomes rise in the developing world. And last year the supply was constricted. China, the world's largest producer of cotton, had production problems, and even during normal years it consumes more of the fibre than it produces. Floods in Pakistan destroyed much of that country's crop. India, in order to keep enough cotton for its own textile mills, announced an export ban.

Some of the gains may have been speculative. Many investors have gone long on commodities: from precious metals to humble grains, most of them had a banner year in 2010. But Gary Adams, the vice-president of economics and policy analysis for the National Cotton Council, reckons that the high prices were mostly due to fundamentals. He points out that cash prices have stayed high, even as futures started to come down at the end of last month, and that most of the cotton is out of the warehouses.

High prices have helped draw attention to some disputes among the states. Texas began gaining ground in cotton production after Australian scientists developed a type of high-quality long-staple cotton called FiberMax. For whatever reason, FiberMax seed fares better in the south-west than in the Deep South, and Texas now produces roughly half of America's cotton. (Last year America produced 18.3m bales-each bale weighing 480lb, or 218kg-and exported more than 80% of them.) Locals in Corpus Christi, a small city on the southern side of the Gulf coast, say this is one reason why their port should become an officially designated delivery point for cotton futures. Francis Gandy, a cotton farmer and member of the Port Commission, argues that once the expansion of the Panama Canal is completed, in 2014, Corpus Christi would be a natural loading-point for cotton shipments bound for Asia.

In any case, cotton prices are likely to stay high for some time. America's farmers will devote more acres to the crop this year, but cotton still has to compete for space with similarly booming crops such as wheat, corn and soyabeans.

That is not a bad dilemma for American farmers. Still, cotton has its troubles. It still has to keep an eye on upstart man-made fibres, such as polyester. And, much more worrying, the textile industry has all but disappeared in the United States. As most of the world's mills are elsewhere, American cotton faces heavy freight charges. But American producers argue that they have a few advantages, such as regulatory predictability and quality control. The country has pretty much defeated the boll weevil, and the Department of Agriculture individually tests every bale on obscure measures such as the tensile strength of the fibres. Foreign textile mills, they hope, have cottoned on to the difference.

The states and their budgets

In search of an answer

Jan 20th 2011 | *CHICAGO* | from PRINT EDITION

Governors, with little in the coffers, start struggling to find money

IN 2010 37 states held elections for governor. It is a wonder anyone wanted the job-most states were submerged in fiscal chaos. Now the messy task of governing begins. Pat Quinn, the governor of Illinois, was one of the few candidates who advocated raising taxes. This month he more than fulfilled his campaign promise. The personal income tax has jumped by a whopping 67%.

States have struggled during the recession, but 2011 may be the most difficult year yet. Easy cuts have already been made. The federal stimulus has given states nearly $200 billion over the past two years; by the end of this fiscal year, aid will all but dry up. Reserves are low: state rainy-day funds have about half as much cash as they did in fiscal 2006. Yet states are likely to face $140 billion in budget gaps by fiscal 2012, according to the Centre on Budget and Policy Priorities, a research outfit in Washington, DC. There is no simple way to close them.

Mr Quinn's approach represents one extreme. The personal-income-tax increase, combined with a higher corporate tax, may delay disaster. The $13 billion deficit in Illinois amounts to about half its budget. But even with extra revenue, problems remain. Since 2009, when Mr Quinn replaced the ineffable Rod Blagojevich, Illinois has borrowed $7.3 billion to pay for its pension system, Medicaid costs and general expenses. The state will soon issue another $4.1 billion in bonds to meet its pension obligations, rather than reform the system. Meanwhile, the new tax may only worsen the state's economic woes. Wisconsin's Republican governor, Scott Walker, welcomed the Illinois tax hike gleefully, inviting businesses to move across the border.

Mr Walker is one of 13 governors who are advocating cuts in spending, and have signed a pledge not to raise taxes. Others have made less formal vows. But keeping them will be hard. In a survey last year by the Pew Centre on the States, about two-thirds of respondents believed that states could provide the same services for less. But trimming waste does only so much. The most costly programmes include education and Medicaid, which voters are loth to cut. As governors unveil their budget proposals, many will try to cut spending and a few may try to raise revenue. The wisest, however, will recognise the unfortunate truth that they must do a bit of both.

Lexington

China in the mind of America

Jan 20th 2011 | from PRINT EDITION

Why some politicians yearn for another "Sputnik moment", and why it wouldn't help



WELL before the presidents of America and China sat down for dinner at the White House on the evening of January 18th, word went out from Barack Obama's people that the very smallness of this working supper marked a new intimacy in relations. Instead of the usual throng of hangers-on, only six diners would be present: Mr Obama and Hu Jintao, with two advisers each (in Mr Obama's case his secretary of state, Hillary Clinton, and his national security adviser, Tom Donilon). This was proof, said the White House, of just how workmanlike relations had become. In two years as president Mr Obama had, after all, had seven previous face-to-face meetings with his Chinese counterpart-and he has met Wen Jiabao, China's prime minister, three times.

That, at any rate, was one of the lines being spun by the Obama administration this week. But as ever where Chinese-American relations are concerned, the messages from the summit were mixed. On the day after their intimate supper, Mr Obama said at a press conference that China's currency was undervalued, and that he had been "very candid" with Mr Hu on human rights, but that China's "peaceful rise" was good for the world and for America. Mr Hu said that China had more to do on human rights, but that relations should be conducted on the basis of "the principle of non-interference in each other's internal affairs". In a formal joint statement China welcomed America as a force for stability in the Asia-Pacific region and America welcomed a "successful China that plays a greater role in world affairs". Both promised more transparent military-to-military ties.

Mixed messages are the stuff of diplomacy, well understood by the leaders on each side. They are certainly nothing to be ashamed of. The inevitable rivalry between America and China is liable to be safer if it is drenched in bromides about how the two countries need not be rivals at all. "Friendly competition", was Mr Obama's phrase this week. But America's politicians do not only send mixed messages to their counterparts in China. They also send mixed messages about China to Americans.

A case in point is the Obama administration's refrain that China's rise presents America with a new "*Sputnik* moment". Mr Obama was not yet born in 1957, when the Soviet Union put the first satellite in orbit around the Earth, but the moment is remembered as a salutary shock to an America grown complacent. Fear of being left behind prompted the federal government to spend hundreds of millions of dollars on scientific and technical education and set up the National Aeronautics and Space Administration (NASA), which in 1969 won the space race by plonking Neil Armstrong and "Buzz" Aldrin on the surface of the moon.

Might competition from China have an equally galvanising impact on the United States? Mr Obama seems to hope so. "Our generation's *Sputnik* moment is back," he said last month: "We need to do what America has always been known for: building, innovating, educating, making things." Steven Chu, Mr Obama's energy secretary, has likewise invoked *Sputnik* to argue that China's investment in clean sources of energy will leave America behind unless America invests in that technology too. John Kerry, chairman of the Senate Foreign Relations Committee, complains that "We've sort of seen *Sputnik* going across the sky, but we've done nothing similar to what we did in the 1960s to respond to it."

The trouble with applying the *Sputnik* moment to China is that it is not much of an analogy. There has, for a start, been no "moment": China has been rising steadily for years without delivering any single shock. Whereas the Soviet Union and America built separate economic spheres, globalisation has bound the American and Chinese economies intimately together, to mutual advantage. And though China is a geopolitical competitor, it is not a mortal enemy of the United States as the Soviet Union was (unlike Nikita Khrushchev, Mr Hu has never promised to "bury" the West). Even if it were, most Americans believe that they still have the military edge. According to a Pew survey, Americans think by two to one (60% to 27%) that China's economic strength is a greater threat than its military might. And a 58% majority says it is very important to build a stronger relationship with China.

A scare story for all seasons

You could argue that to invoke *Sputnik* is merely to say that America needs to wake up and take remedial action. But harking back to *Sputnik* is hardly consistent with "friendly competition". And where is the point in stoking up fear of China if Americans cannot agree on what to do about it? It may have seemed obvious after *Sputnik* that America should make a big public investment in technology. No similar consensus applies today. Though Mr Obama wants to invest in clean technology, other Democrats see protectionism as the answer to China. As for the Republicans, they too point to China as a reason for America to try harder. Newt Gingrich, one of their presidential possible wannabes, calls the possibility of America falling behind China in technology one of the "potentially catastrophic threats" facing the country. But his remedies emphasise tax cuts, a smaller state and freer markets, not the public investments Democrats favour.

It is not hard to see why the *Sputnik* era appeals to Mr Obama. For all the talk they hear about China's headlong investment in infrastructure, American voters are lukewarm about their own government's spending, especially if debt or taxes must rise to pay for it. A new *Sputnik* moment might change their minds. But in the 1960s Americans were sure their system could deliver the goods. Today they are perplexed by the success of China's model and divided on how, if it is even possible, to restore the health of their own. They should resolve that quarrel on its merits and keep the China scare out of it. Apart from anything else, that might improve the atmosphere at the next presidential dinner.

Economist.com/blogs/lexington

Index | The Americas

Organised crime in Central America

The rot spreads

Jan 20th 2011 | *SAN SALVADOR* | from PRINT EDITION

Drug-trafficking gangs find a promising new home in some of the poorest and most vulnerable countries in the Americas



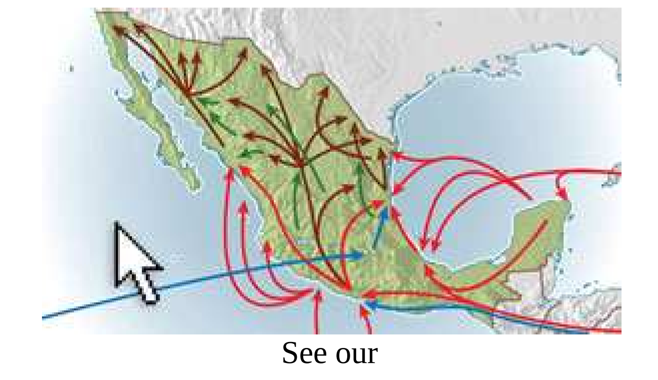
BATTLEFIELDS aside, the countries known as "the northern triangle" of the Central American isthmus form what is now the most violent region on earth. El Salvador, Guatemala and Honduras, along with Jamaica and Venezuela, suffer the world's highest murder rates (see map). The first two are bloodier now than they were during their civil wars in the 1980s.



Organised crime is now the main cause of the bloodshed. Central America forms a bridge between Colombia, the world's biggest cocaine producer, and Mexico, which is the staging post for the world's biggest market for the drug-the United States. As pressure has mounted on the mobs, first in Colombia and now in Mexico, Central America has attracted more traffic. Ten years ago it had fewer cocaine seizures than either Mexico or the Caribbean; by 2008 it accounted for three times more than both combined. Over the same period the murder rate rose across the region, doubling in some countries.

"Central America is entering an extraordinarily critical phase" in which its peace and security are threatened by "the onslaught of the drug-trafficking organisations", an official from the International Narcotics Control Board, a United Nations agency, warned this month.

Much of the blame lies with the arrival of the Mexican mafias, mainly the Zetas and the Sinaloa "cartel". The assassination of Honduras's top anti-drugs official in 2009 seems to have been a Sinaloa hit. Zeta training-camps and recruitment banners have sprung up in Guatemala. The Mexican mobs are also contracting out their work, taking advantage of Central America's competitive narco-labour market. They recruit trained hitmen from the pool of soldiers laid off by several countries' armies, slashed since the end of the civil wars 20 years ago. Guatemala has cut its army's nominal strength by two-thirds since 1996. Now former members of its notorious Kaibiles special forces are said to have close links with the Zetas, themselves a former Mexican special-forces unit.



See our

Then there are the roughly 70,000 members of Central America's *maras*, or youth gangs, which provide a ready supply of teenagers willing to ferry drugs, mind kidnap victims and carry out other low-level tasks. The blossoming links between the drug traffickers and the *maras* are a big worry. "What would happen if the cartels infiltrated and united with the *maras*? There would be war, as in the *favelas* [self-built settlements] of Rio de Janeiro," says Alejandro Gomez Vides, president of the Central American Court of Justice.

Leave aside that nowadays Rio looks peaceful compared with parts of Central America. There are signs this fusion is already happening. In El Salvador the proportion of crimes attributed to minors rose from 5% in 2000 to 12% in 2009, and the number of imprisoned youths more than doubled in that period. Mexican mobs have found the *maras* to be "fertile ground", says Aida Luz Santos de Escobar, president of El Salvador's public-security council, a government agency. In the *maras* they have found "people who don't value life, nor even their own liberty," she says. The Mexicans' tendency to pay in drugs has pushed up local consumption, offering new opportunities for criminality.

Most Central American governments are ill-equipped to tackle the mayhem. The countries of the "northern triangle" are among the poorest in the Americas, with income per head of around $2,700, less than a third that of Mexico. The $2.1 billion of drugs, arms and cash recovered in Guatemala during the first six months of last year was equivalent to 5% of the country's GDP. Yet despite its poverty, Central America receives little outside help: of the $1.6 billion so far allocated under the Merida Initiative, a United States drug-fighting programme for Mexico and Central America, Mexico received 84%.

Political instability adds to the difficulties. Nearly all foreign aid to Honduras, as well as intelligence-sharing, was frozen following a coup against its president in 2009. One result has been a rise in drug flights from Colombia and Venezuela to Honduras, according to a report from the Wilson Centre, a think-tank based in Washington, DC. At least 154 such flights were logged in 2009, compared with almost none in 2005. A new government has since restored some of Honduras's international ties, and the flights have tapered off. But some American congressmen want to cut aid until human rights are respected.

Though Central America offers a new base for Mexican traffickers, it could yet be their undoing. Mexico's cartels, now the most powerful in Latin America, began as runners for the Colombians and were paid in product. They promptly seized control of distribution in the United States, and turned the Colombians into mere suppliers. The *maras* of Central America, which have close ties to inner-city gangs in *el norte*, could yet pull off the same trick. Roy David Urtecho, Honduras's attorney-general, recently warned that the *maras* were seeking "to establish themselves as legitimate traffickers instead of street-level thugs". The battleground in the war on drugs may be about to shift again.

Index | The Americas

The coca leaf

Storm in an Andean teacup

Jan 20th 2011 | *MEXICO CITY* | from PRINT EDITION

A battle over mastication

TOURISTS who visit Bolivia's capital, La Paz, or Cusco, Peru's former Inca seat, are routinely given welcome cups of coca tea to mitigate *soroche* (altitude sickness). For centuries, people who live in the high Andes have chewed coca leaves, whose alkaloids act as a mild stimulant and help to ward off cold and hunger. The Spanish conquistadors declared coca a tool of the devil, until they saw how it improved the work rate of the Indians they sent down the mines.

But refine the alkaloids in coca, and you get cocaine. In 1961 a United Nations convention on narcotics banned the leaves, giving countries 25 years to outlaw this ancestral practice. Half a century on, consuming coca remains legal in Bolivia, Peru, Argentina and some parts of Colombia, in defiance of the convention. In Bolivia and Peru, some cultivation is legal too. In 2009 Bolivia, where a new constitution protects coca as part of the country's cultural heritage, proposed an amendment to the convention that would remove the obligation to prohibit traditional uses of coca. Other South American countries agree.

The amendment would have passed if no objections were raised by the end of this month. But this week the United States spoke up, probably scuppering the change. The European Union (at Britain's behest) may follow. They argue that tolerating the use of coca harms efforts to suppress cocaine. Bolivia insists it would continue to fight cocaine and limit coca cultivation. But cultivation in Bolivia and Peru has long outstripped traditional use, and is rising sharply.

Yet this smacks of hypocrisy. The United States' State Department's website recommends coca tea for altitude sickness, and its La Paz embassy has been known to serve it to visitors. The UN's declaration on indigenous peoples, which the United States endorsed last month, guarantees the protection of "cultural heritage, traditional knowledge and traditional cultural expressions".

"It's clear to me that some people there [in the State Department] realise it's senseless to continue the war on drugs," says Fernando Henrique Cardoso, a former president of Brazil who wants marijuana decriminalised and is chairing a commission on drug policy worldwide.

But the drug warriors in the American administration seem to have prevailed over the diplomats. Bolivia is considering pulling out of the convention if its modest proposal is struck down. The State Department has been trying to repair ties with Bolivia's socialist government since a spat in 2008 in which ambassadors were expelled. But all too often American policy towards Latin America has been dominated by drugs.

Index | The Americas

Disaster prevention in Brazil

After the flood

Jan 20th 2011 | *RIO DE JANEIRO* | from PRINT EDITION

Why did so many die?



Better to rebuild somewhere safer

FOR two centuries the mountains behind Rio de Janeiro have been the perfect Brazilian getaway. Pedro II, a 19th-century emperor, would decamp there with his court to escape Rio's sweltering summer heat. More recently Rio's rich have done the same, carving weekend palaces from the sheer granite walls and dense forests shouldering towns with noble names like Petropolis, Teresopolis and Nova Friburgo. Settled by German and Swiss immigrants, these once-quaint villages of gingerbread architecture have turned into bustling cities. Now they are a shambles.

This week rescue workers continued to dig in the wreckage after violent summer storms dumped more than a month's worth of rain on the sheer slopes of Rio's *serra* in hours, unleashing what officials have called a "tsunami" of mud. At least 740 people are known to have died, more than 200 are missing and 21,500 are homeless. Drinking water, electricity and telephone lines have largely been restored. But a dozen villages were still cut off. With farms buried by mud and rock, Rio has lost its most reliable source of fruit and vegetables, sending their price rocketing.

As the rains abate, for now at least, the political deluge has begun. Rio's tragedy was linked to La NiÃ±a, a periodic cooling of the eastern Pacific which affects weather around the world. Catastrophic rains have become more frequent in Brazil (and elsewhere). But much of the blame for the high death toll lies closer to earth. Brazil has sophisticated satellite technology, able to pinpoint forest fires and tree-cutting and to predict the weather. Yet each storm seems to catch officialdom off guard.

Part of the problem is the rapid growth of the mountain region, now home to 600,000 people. A nascent textile industry there beckoned migrants in the 1980s and 1990s. On their heels came wealthy *cariocas* (as residents of Rio are called), who started a property boom in weekend homes. Since labour chases wealth, soon the mountain towns were brimming with *favelas* (self-built settlements), hurled up haphazardly on treacherous slopes.

Rodrigo Neves, Rio state secretary of social assistance and human rights, declared that 5,000 families must move to safer ground at once. And Rio's *serra* is the least of Brazil's disaster problem. All told, 5m Brazilians live in danger zones, at the mercy of rogue weather, according to Aloizio Mercadante, the science minister.

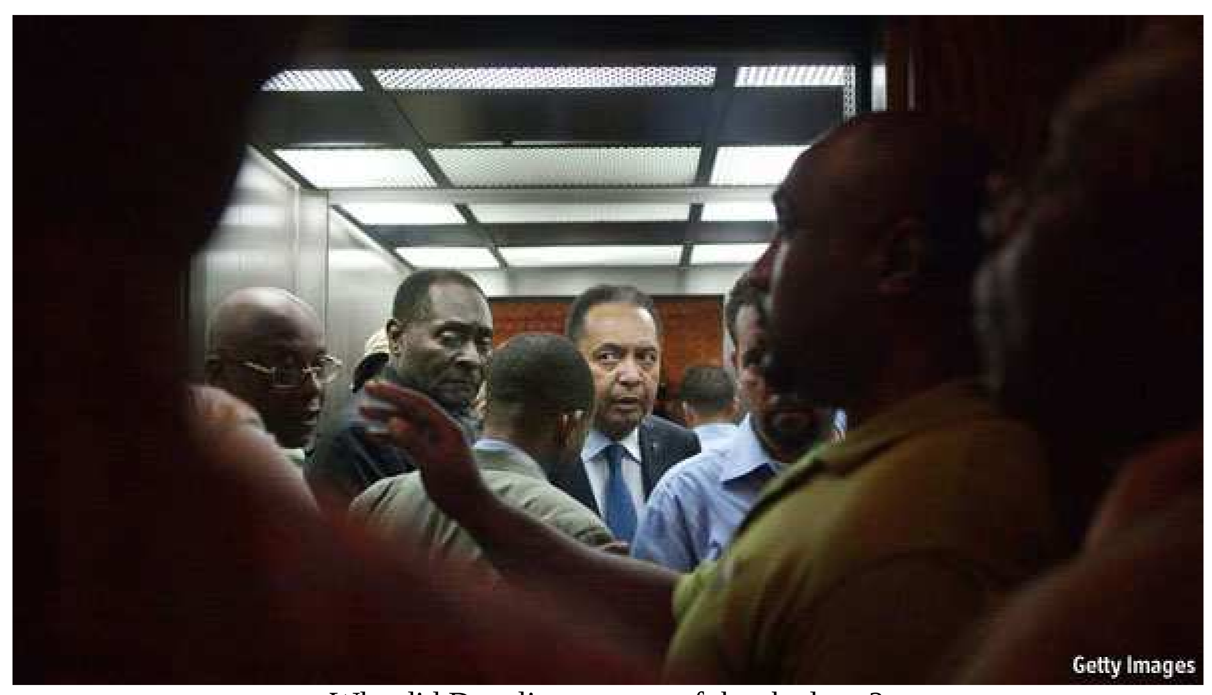
Disaster relief trumps disaster prevention in Brazil. Though the federal government budgeted 442m reais ($263m) for disaster prevention last year, only 139m reais was in fact spent, according to Contas Abertas, a watchdog group. Less than 1% of money for preventive works in a big federal investment plan (called the PAC) found its way to flood-prone Rio de Janeiro state last year. The federal government says that is because few towns presented workable projects. But remarkably, Bahia state alone got 54% of this disaster fund. It happens to be the political home of Gedel Vieira and Joao Santana, both formerly ministers of national integration (which includes civil defence) and both chiefs of the Party of the Brazilian Democratic Movement, a powerful government ally. If lessons are to be learned from Rio's tragedy, the place to look is not in the clouds.

Justice and Haiti

Baby crawls back

Jan 20th 2011 | *PORT-AU-PRINCE* | from PRINT EDITION

A former dictator's ill-timed return



Why did Duvalier step out of the shadows?

IS THERE such a thing as a crime in Haiti? The surprise return to the country this week of Jean-Claude Duvalier, nearly 25 years after he left for exile in France, may answer that question. Though "Baby Doc" was a less brutal dictator than his papa, Francois, a doctor, his regime featured torture and corruption. Human-rights groups say he fleeced the Haitian treasury of at least $300m. Several hundred political opponents disappeared; others were ill-treated in Fort Dimanche, his grim jail.

For most of the period since Mr Duvalier's overthrow in 1986, Haiti has experienced a chaotic democracy, instability and economic stagnation. So some older Haitians look on the Duvaliers with nostalgia. Most do not. For what remains of the country's intelligentsia, the return of the wide-eyed, stooped and sallow-faced dictator was almost as unsettling as the 47 seconds this time last year when the earth shifted and buckled under their feet.

Mr Duvalier's scheduled press conference was replaced by a visit to the prosecutor's office. After several hours of questioning he was charged with embezzlement and corruption, and then released to return to his posh hotel. A judge now has three months to decide whether there is enough evidence for a trial. Human-rights groups want Baby Doc tried for abusing people as well as money, and some of the victims have begun filing complaints.

All this comes at an especially awkward time for Haiti. This week the Organisation of American States was negotiating with Rene Preval, the outgoing president, and the electoral authority over which two presidential candidates should contest a run-off election, postponed from January 16th after the official count was disputed.

Was it chance that Mr Duvalier turned up on that very day? One conspiracy theory holds that his arrival was arranged by Mr Preval as a coded threat to outsiders that rather than contemplate the defeat of his chosen successor he might arrange the return of a more popular exiled former president, Jean-Bertrand Aristide, a leftist whose corrupt misrule prompted his controversial ousting in 2004. Mr Aristide said he was "ready" to return from South Africa. Aid donors think that would add to Haiti's many problems. On this matter, like others, Mr Preval is silent.

But the most plausible motive for Mr Duvalier's visit is that he hopes to get embezzlement charges dismissed in Haiti before they are heard in Switzerland, where the authorities have frozen about $5m that he holds. A new law, which comes into force on February 1st, would allow Swiss prosecutors to bring a case against Mr Duvalier and return the money to Haiti if he loses. With nearly 1m earthquake victims still displaced, a cholera epidemic and a political vacuum, Haiti faces many pressing tasks. Judging Mr Duvalier has just joined the list.

Index | The Americas

Cuba and the United States

The worm that turned

Jan 20th 2011 | *HAVANA* | from PRINT EDITION

Helping Cubans to help themselves

AMERICAN presidents tend to be very cautious when it comes to policy toward Cuba. True to form, Barack Obama's latest directive relaxing the rules on travel and remittances to the communist island was released late on January 14th, just before a long weekend. The directive makes it easier for religious, cultural and educational groups to visit, widens the number of airports which can apply to host charter flights and allows all Americans to send up to $2,000 a year to ordinary Cubans.

The broader economic embargo against Cuba stands. Only Congress can scrap it, and many in the new Republican majority still support it. But the administration has taken a further step in reversing George Bush's tightening of the embargo.

In 2009 it abolished Mr Bush's curbs on travel and remittances by Cuban-Americans. That has already had a noticeable effect. Last year some 400,000 Americans visited Cuba, the highest figure since before the 1959 revolution. The United States now ranks second to Canada as a source of visitors, even though direct flights have been allowed only from Miami, New York and Los Angeles and are usually full. Remittances from across the Florida Straits may amount to $1 billion a year. Havana's best nightclubs and restaurants, once the preserve of foreigners, are now full of Cubans and their Cuban-American hosts.

Cuba's government called the latest directive "positive" but "limited". Some Cuban-American leaders denounce the changes as simply propping up the Castro brothers with American dollars. But the administration says they are designed to help Cubans free themselves from the communist state.

Allowing Americans without relatives on the island to send money will help to promote "private economic activity". The directive comes as Raul Castro, Cuba's president, has launched a reform of the island's stagnant economy under which up to 1.8m, from a workforce of 5.2m, will be laid off from state jobs over the next few years, and required to make a living from self-employment or small business.

These people will need capital. Cuba's Central Bank may provide loans. Spain and Brazil have expressed interest in helping. But the most likely source of funds will be relatives abroad. Not long ago any Cuban leaving the island was denounced as a *gusano* (worm). No wonder that word has been officially retired.

Index | Asia

Integrating South-East Asia

China coming down the tracks

Jan 20th 2011 | *BANGKOK* | from PRINT EDITION

A railway boom promises to tie South-East Asia together-and boost China's sway



THE rapid expansion of its high-speed railways has got China plenty of attention. Yet ambitions do not stop at the border. On its southern flank China is renewing a push to lay tracks to mainland South-East Asia. The region's leaders have dreamed since the 1990s of seamless rail travel between Singapore and Kunming, capital of the south-western Chinese province of Yunnan. South-East Asia's existing network of railways is creaking, patchy and underfunded. Most goods move about the region by lorry and ship. But that creates choke points while running up fuel bills. An integrated rail system could be just the ticket.

Enter China, chequebook in hand. It has recently signed agreements to build new lines in Laos and Thailand, while it extends its network from Kunming to the China-Laos border. These lines are meant to be ready by 2015. The benefits may be huge. Most countries along the route have already hitched their wagons to China's outsize economy and are eager for more trade. China's free-trade agreement with the Association of South-East Asian Nations (ASEAN), which took effect a year ago, has cut tariffs on most traded goods. The region still has natural resources, which China is keen to strip.



Empire-builders love railways. Most of South-East Asia's were laid during colonial rule, as Britain and France pushed inland. In a region with American leanings, China wants to bind its neighbours into an economic sphere with strategic weight. Laying lines into Myanmar, with a large but decrepit network, would add a coveted Indian Ocean port. More

regional trade with its centre in Yunnan spreads wealth inland, another Chinese objective. Trains already shuttle between China and Vietnam, which has a north-south railway. This linkage opens up the possibility of a circuitous eastern route into South-East Asia, via Cambodia and Thailand. Both countries belong to the Greater Mekong Subregion, a grouping fostered by the Asian Development Bank (ADB) that also includes Vietnam, China, Laos and Myanmar. According to the ADB, it would cost $1.1 billion to build the missing links along this route, making it the cheapest way to connect the region. Some $7 billion more would be needed to upgrade existing lines and rolling-stock. By 2014, once this route is operating, it would carry almost 7m tonnes of cargo among Greater Mekong countries, rising to 26m tonnes by 2025, the ADB reckons. Greater Mekong countries duly backed the plan in August.

Yet China quickly upended this consensus. In December Laos said China would build a $7 billion high-speed railway from the border to its capital, Vientiane. Construction is set to begin in April. Meanwhile, Thailand is negotiating with China to build a connecting north-south line to Bangkok, using concessionary Chinese loans. ADB officials are left scratching their heads over what this means for the Vietnam-Cambodia route, including a long stretch that China had been expected to build but which now appears to be on the back burner.

On paper, the Laos-Thailand route is more direct, but it is also far more mountainous, with 190 kilometres (120 miles) of tunnels in Laos and countless bridges. Remote areas of Laos are also littered with unexploded bombs from the Vietnam war. None of this is likely to stop a country that laid a railway up to the Tibetan plateau.

In Thailand the hazards are more political. To get around the mighty, hidebound state operator, the Thai government proposes a new line using Chinese technology to run parallel to the existing one. A Thai-Chinese entity would rent the land from the state operator and build its own signals and stations. Handily, the route would pass through Thailand's poor and politically disaffected north-east, giving a shot in the arm to the local economy.

Thailand says that fast passenger trains would reach speeds of 200 kilometres an hour, streets ahead of what currently pass for express trains. Tourists could ride luxury carriages to exotic destinations. A fast train, says Korbsak Sabhavasu, the government's chief negotiator, is something Thailand needed 20 years ago. But Thailand's treacherous politics may yet intrude, as any final agreement with China needs the nod from parliament. In an election year, this is no certainty.

Tourists and trainspotters may be tickled by a fast train to China. Yet the real point of modernising the railways is cargo. Intra-ASEAN trade is growing much faster than exports to developed markets. Nearly a quarter of Thailand's exports go to South-East Asia, with another 11% (and rising) to China. Trains are more efficient and less polluting than lorries on all but the shortest routes. Peter Broch of the ADB estimates that a rail service from Bangkok to Phnom Penh would cut the price of moving a container by two-thirds compared with moving it by ship and lorry, as now.

Even without a railway network, the region is tying itself together. Roads have been upgraded, and customs procedures are less tape-bound than they were before. When Wang Er-Chern began trading agricultural produce in northern Thailand in the early 1990s, it took two weeks to send goods by road and ship via Laos to his native Yunnan. Today the journey has been shaved to two days. Mr Wang, prominent in the Thai Yunnan Commerce Association, says a fast rail link to Kunming would be nice. But he grumbles that business has already become less profitable as more Chinese traders have got in on the act. A trainload more may soon be on the way.

Index | Asia

A cabinet shake-up in Japan

The pol who won't give up

Jan 20th 2011 | *TOKYO* | from PRINT EDITION

Naoto Kan's new steward of economic reform, with his old tax message



Do you mind if I raise taxes?

"DO YOU mind if I smoke?" rasps Kaoru Yosano, 72, a survivor of throat cancer. Mr Yosano is no quitter. At an age when, even in Japan, many politicians bow out, on January 14th he performed a flying trapeze act by joining the government of Naoto Kan, whose Democratic Party of Japan (DPJ) he has derided for years.

A year ago, when the DPJ's Yukio Hatoyama was prime minister, Mr Yosano wrote a book called "The DPJ Destroys Japan's Economy". But that was before Mr Kan took over with the (for Japan) radical promise of launching debate on raising the consumption (ie, sales) tax, which at 5% is the lowest in the rich world. The promise nearly sank Mr Kan, but it endeared him to Mr Yosano. Now the former finance minister (and grandson of two famous pre-war poets) has become Mr Kan's man on tax and pension reform.

It is a gamble. Mr Yosano's appointment offended many in the opposition Liberal Democratic Party (LDP) that gave him a seat in 2009 out of loyalty (ironically, he had lost his Tokyo constituency to the DPJ's Banri Kaieda, whose job in the cabinet he has just taken). Some LDP members may try to blackball Mr Yosano in the Diet (parliament). He has few natural allies in the DPJ, and does not disguise his differences. At heart he believes, perhaps hopes, the LDP can return to power, if only it reforms itself.

Yet Mr Yosano's appointment is bold, too. Even his critics acknowledge that, in taking the job at his age, he is driven more by principle than glory. He believes in urgent tax reform if fading Japan is to shore up pensions, health-care and child-support systems. Mr Kan, whose party lacks a majority in the upper house, needs more such opposition politicians. Mr Yosano may be a good model.

The new minister is still coy about how much the consumption tax should be raised. Like Mr Kan, he appears to think doubling it would be a start. Opponents say that would derail a fragile recovery. But Mr Yosano says that, on the contrary it would give people confidence about the solvency of the pensions system, which would encourage them to spend. He also believes the markets need reassurance about the health of all public finances, which he describes as "far worse than in a few of the worst European countries" (gross debt is twice the size of GDP).

On the timing of a tax rise, opinions in government vary. Koichiro Gemba, Mr Kan's main policy adviser, says a rise in the consumption tax should not be before the next general election, though cross-party talks should start within the next five months, with a tax increase decided by March 2012. Mr Yosano remains non-committal.

In Japan the media and the opposition seize on such differences as evidence of disarray. Yet, with a reshuffled cabinet, the government at last appears to have settled on a message of reform, including of trade and agriculture, that appears

refreshingly non-partisan. Among other things, Mr Kan wants a decision by June on whether Japan should begin trade talks, including with America, under the aegis of the Trans-Pacific Partnership, a free-trade block.

For now, squabbling or even gridlock will mark the Diet at least until the spring. The opposition looks determined to try to block Mr Kan's budget, believing the tactic will score points in prefectural and municipal elections in April. But if Mr Kan can ride that out, with public opinion on his side he may yet persuade opponents to support policies that start dealing with the country's troubled finances. Japan's economy, Mr Yosano once wrote, was infected with a grave cancer. The inveterate smoker is now Mr Kan's chief ally in cutting it out.

Index | Asia

Indian politics

More bite needed

Jan 20th 2011 | *DELHI* | from PRINT EDITION

A cautious prime minister is letting his second term drift away



Fuel hikes fan the flames

TWO chapatis and a dollop of dal is said to constitute lunch for Manmohan Singh, the prime minister. The gentle, brainy fellow, at 78, remains alert and industrious. He is considered honest and frugal, rare virtues in a country with eye-popping graft.

Yet Mr Singh could do with a new-year menu of meatier fare. He has been passive in the face of recent setbacks. Corruption scandals forced out two of his ministers, with a third redeployed. The opposition Bharatiya Janata Party (BJP), demanding a public inquiry on graft, blocked Parliament throughout the winter session and may do so again in spring.

The Supreme Court has chided Mr Singh for dragging his feet over a scam at the telecoms ministry costing probably billions of dollars. And on January 17th prominent types decried in a public letter a "widespread governance deficit". A cabinet minister says all this hurts.

Mr Singh's main response has been a shrug and a twinkly smile. He won a second term in 2009 with the strongest mandate of any prime minister in the past 20 years. The opposition, at least until it rallied around the cause of corruption, has been unfocused. Yet Mr Singh's second government has offered no big policy reforms, while letting public support ebb away as voters grumble about graft and inflation. On January 19th a modest cabinet reshuffle took place. Mr Singh has since promised a "more expansive exercise" after the budget next month.

Mr Singh describes himself as an "accidental politician", and he will anyway be gone before the next election, probably in 2014. It is more baffling that Sonia Gandhi, the real power behind the Congress Party, which dominates the government coalition, does little to stop the drift, especially given Congress's recent electoral setbacks in important states, notably Bihar. Mrs Gandhi's son, Rahul, is the most likely choice as the next prime minister, though he did not take a government job in this week's reshuffle. Mr Gandhi's efforts to get young, rural voters to turn out for Congress have been disappointing. While touring Uttar Pradesh this month, his car was battered by angry youths. His recent attempt to blame government woes on coalition politics looked limp: Mr Singh's government is unusually secure in Parliament.

Congress has time to fix its problems. And despite the drift, some ministers, notably the environment minister, Jairam Ramesh, have an eye for the popular gesture. This week he ordered a scandal-tainted apartment block in Mumbai to be razed. Meanwhile, the Supreme Court is pushing against corruption. On January 19th it asked the government to release more details on how rich Indians stash money abroad to evade taxes.

The most pressing task is to ensure a healthy economy. Though economic growth, at an annualised rate of 9%, remains robust, foreign investment has fallen and growth in industrial output has slowed. Now inflation is surging. Fuel prices are higher after the government boldly scrapped subsidies on petrol and diesel. Food inflation, at 17%, is even more painful and may now bring protesters into the streets. Poorer Indians are furious at stinging prices for onions and pulses such as the lentils favoured by Mr Singh.

The government has few options to deal with this quickly. Dearer food in India is mainly a reflection of rising commodity prices around the world. But the government could tackle home-grown difficulties that strangle supply in all sorts of industries, including agriculture, retailing, infrastructure and logistics. Allowing in more foreign investors would help keep the economy charging on. Yet the liberal Mr Singh, once the architect of Indian reforms, appears not so bold as he was.

Index | Asia

Reporting in North Korea

Not the Pyongyang Times

Jan 20th 2011 | *SEOUL* | from PRINT EDITION

Journalism that carries the death penalty

THE only publication written by North Koreans, about North Korea, for consumption by the outside world, is named after a river that flows from the North to South Korea and into the Yellow Sea. *Rimjingang*'s eight reporters are dotted about the totalitarian state; their backgrounds range from factory work to the civil service. In China they were trained in undercover recording techniques. And then they went home to begin their work. If caught, they surely face death.

Their reports are smuggled back into China, and then to Japan, where the magazine's publisher, Asiapress, is based. *Rimjingang* produced a shocking video late last year of a homeless young woman, her face blackened with dirt, foraging on a mountainside. Images of the woman, who may have died soon after, went around the world.

Rimjingang is emblematic of the challenges to the regime of Kim Jong Il posed by technology. Reports can be carried across the border on memory sticks, or transmitted via Chinese mobile phones that pick up signals on the North Korean side of the Yalu river.

Rimjingang, and a publication about North Korean conditions by a Buddhist aid group, Good Friends, have been exceptions. Most of the information that flows is inward, from outsiders countering state propaganda and hoping to foment anti-regime sentiment. Open Radio for North Korea, founded five years ago in America, combines Korean pop with human-rights information.

Open Radio, though, is starting to find ways to work in both directions. A month ago, the station broke the story that a train bound for Pyongyang containing gifts from China for Kim Jong Un, the heir-apparent, was sabotaged and derailed. The source was apparently an official from North Pyongan province, the region in which the incident occurred. Last March Free North Korea Radio claimed to have equipped three North Koreans with satellite phones, which offer a lower risk of detection.

Perhaps the greatest force for change remains pirated DVDs from China. Though not a part of any deliberate effort to subvert the system, they mean that nearly everyone has seen South Korean soap operas and knows how prosperous Seoul really looks. "Fear still rules," says a defector. "But people know more about the world than you might think."

Index | Asia

Politics in Malaysia

Najib in overdrive

Jan 20th 2011 | *KUALA LUMPUR* | from PRINT EDITION

Early elections are a possibility

IT IS rare when a few days pass without the prime minister, Najib Razak, announcing new and sometimes not so new projects under his vaunted Economic Transformation Programme (ETP). Last week saw 19 of them, from building a new "World-Class Data Centre Hub" to the creation of the Talent Corporation, "tasked to strategise and implement initiatives" to fill millions of supposed new jobs. Few areas of life are spared and acronyms and abbreviations proliferate. Thus a Wellness City is planned, and seven types of "high-demand" herbs will be cultivated under the aegis of the ECER, which, for those who have not kept up, is an NKEA in the ETP, the whole to be overseen by PEMANDU. You can, inevitably, follow it all on Twitter.

Mr Najib says the ETP is starting the year "with a bang by switching into overdrive", part of a wider modernisation to win the Malaysian economy rich-world status by 2020. Yet the rush also looks part of a very different strategy: to win a general election which the prime minister may call this year, perhaps as early as in the spring, despite not having to go to the polls until 2013.

It reflects Mr Najib's political weaknesses as much as his strengths. He did not win his mandate as prime minister at the polls. Rather, he owes his position to an internal coup within the ruling party, the United Malays National Organisation (UMNO), that saw him take over from his former boss, Abdullah Badawi, in April 2009. Mr Badawi was blamed by party bigwigs for the big losses that UMNO suffered at the general election in 2008. The party, the biggest in a coalition called Barisan Nasional (BN), retained power, but for the first time since independence in 1957 the BN lost its two-thirds majority in Parliament. Although the government could now hang on for another two years, Mr Najib seems to want his own mandate from the electorate before then, if only to face down many in his own party who are hostile to the direction in which he wants to go.

UMNO was founded to protect the interests of Malays and other indigenous peoples, who make up about two-thirds of the population, against those, mainly Chinese and Indian, who arrived under British rule in the 19th and 20th centuries. At independence these people were given citizenship, but in exchange Malays were granted special "privileges" to protect their political power and assure a larger share of the country's wealth. These days, many argue that all the quotas and affirmative-action programmes to help the Malays are now not only obsolete, but counter-productive. Maintaining quotas for Malays in some universities, for instance, drives the brightest ethnic Chinese abroad. Often they do not come back, and the economy suffers from the loss of their entrepreneurial skills-they make neighbouring Singapore even richer instead.

Mr Najib broadly agrees. At the heart of his ETP is a pledge to introduce a more meritocratic society. Being a cautious politician, however, he hedges his message with promises not to abolish all the rights of the *bumiputra* ("sons of the soil"), as his core Malay constituency is called.

Nonetheless, for some in his party and the government bureaucracy (staffed largely by ethnic Malays), he is still going too fast, or even in the wrong direction. Wan Saiful, head of the Institute for Democracy and Economic Affairs, points out that the new policy is being promoted mainly by bodies, including the ETP, which have been set up within the prime minister's office rather than in the relevant ministries. It is a sign, he says, that the cabinet is not buying into Mr Najib's ideas. Further, Mr Najib has to contend with a ginger group, Perkasa, that claims to defend Malay rights within UMNO.

The next election, says one of Mr Najib's former advisers, will thus be presidential in character. It will be a test of Mr Najib's ability to assert his agenda within his own party and government as much as a fight against the opposition, a coalition led by Anwar Ibrahim's People's Justice Party.

The prime minister's men are tracking the polls carefully, and are encouraged by recent by-election victories. Mr Najib will have to win big to convince the sceptics, at the very least restoring the BN's two-thirds majority. Should he do that, he will be able to sweep out the UMNO old guard. Only then will it be clear what a previously unassuming technocrat with modernising ideas can do to transform his country.

Index | Asia

China's Confucius Institutes

Rectification of statues

Jan 20th 2011 | *BEIJING* | from PRINT EDITION

Confucius as soft power, but the message gets confused at home



A WEEK before President Hu Jintao's visit to America on January 18th the appearance of a giant bronze statue of Confucius on the east side of Tiananmen Square caused a stir in the Chinese capital. He is the first non-revolutionary to be commemorated on the hallowed ground of Chinese communism. The party, having once vilified the ancient sage, now depends on him in its attempts at global rebranding.

Mao Zedong, the only other figure permanently honoured at Tiananmen (a portrait of Sun Yat-sen is displayed twice a year), is considered a bit too controversial among foreigners to be part of this image-moulding effort. In 2004 China began

setting up language schools abroad to extend its cultural reach. They were called Confucius Institutes, apparently to boost their appeal by disguising any links with communism.

During his trip to America, Mr Hu hopes Confucius will help him connect with ordinary Americans. His itinerary includes a visit to a high school in Chicago that is home to a Confucius Institute. Of about 320 such institutes worldwide, over one-fifth are in America. The United States is also home to more than 200 offshoot "Confucius Classrooms".

China has been careful not to encourage these language centres to act as overt purveyors of the party's political viewpoints, and little suggests they are doing so. But officials do say that an important goal is to give the world a "correct" understanding of China. An online Confucius Institute, also supported by the Chinese government, includes an article noting the "active" efforts of some unspecified Confucius Institutes in opposing independence for Tibet and Xinjiang, pro-democracy activism and the Falun Gong sect.

Promoting Confucianism is not part of their remit. Party officials use Confucius as a Father-Christmas-like symbol of avuncular Chineseness rather than as the proponent of a philosophical outlook. (Mao was more concerned with the philosophy, which he rallied the nation to attack as a legacy of the bad old days.) The new Confucius statue, on the other hand, appears to have struck a wrong note. Of more than 820,000 responses to an online poll conducted by the party newspaper, the *People's Daily*, 62% opposed it. Mr Hu's efforts at rebranding need some more explaining at home.

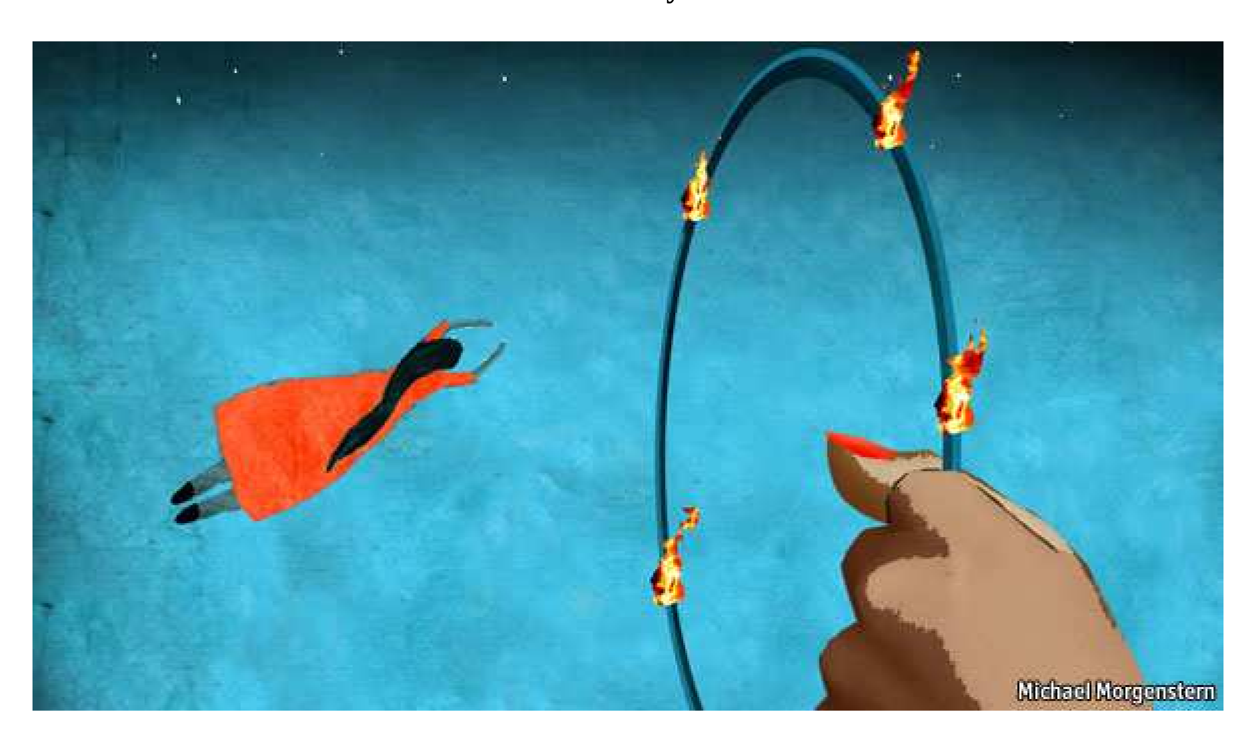
Index | Asia

Banyan

Tiger cubs v precious lambs

Jan 20th 2011 | from PRINT EDITION

The contest with China moves into the classroom and nursery



SOME 2,400 years ago Mencius, a Confucian sage, endured a peripatetic Chinese childhood. His tigerish mother moved house three times before settling on one good enough for the infant genius-close to a good school. Many modern parents, anxious to give their child a winning start in the postcode lottery of life, would sympathise. They agonise about how to raise their children. Chinese mothers, however, still know what's best.

So contends Amy Chua, a Chinese-American law lecturer, who has whipped up a storm with her book "Battle Hymn of the Tiger Mother", and, in particular, a provocative extract published in the *Wall Street Journal*. The article's starting-

point is that "Chinese parents raise such stereotypically successful kids", because "Chinese mothers are superior". Chinese matriarchs are better because they are tougher, stricter and readier to be loathed for banning children from almost any form of fun, from play dates to-horrors!-computer games. Indulgent Western parents, cosseting their baa-lambs' self-esteem and releasing them to play in the mud when they could be doing extra arithmetic or practising scales, are condemning them to a life of underachievement.

Criticising someone's fitness as a mother is worse than calling her a bad driver. Doing it on a continental scale is bound to upset-especially, during a vogue for scare stories about China's rise, when the critic is Chinese (or in this case, an American, who was born in America to immigrants from the Philippines, yet considers herself Chinese). One of the many fields where the West is conscious of heightened Chinese competition is education.

In December the OECD published the results of a test pitting teenage students around the world against each other in reading, science and maths. Shanghai students comfortably pipped the South Koreans, Singaporeans and Hong Kong Chinese, with only eccentric Finns bucking the Western-slacker trend. America was 17th in reading and even lower in maths and science.

The results will not have surprised the creator of a self-explanatory American website, Asians Sleeping in the Library, "meant to celebrate...the hardest workers at our universities." Recent research in Sydney, Australia showed that diligence begins early: primary-school children from Chinese backgrounds spent an hour doing homework every night of the week, compared with 20 minutes some nights for Anglo-Australians. In Singapore Chinese children do notably better academically than the Malay and Indian minorities, though the reasons why are disputed.

Nicholas Kristof, writing in the *New York Times*, called "the rise of China's education system and the passion for learning that underlies it" the "real challenge" the country poses America. In the light of such misgivings Ms Chua's rant was bound to raise hackles in America and other centres of permissive parenthood. Even her own book questions the article's claim that Chinese mothers are better. But she has also offended many Chinese, especially in America, who do not identify themselves with her form of extreme parenting. Blogs have written of young people driven to suicide by the pressure to succeed (though suicide rates among Asian-Americans are not abnormally high).

Most commentators seemed to accept Ms Chua's premise about Chinese mothers' approach, if not its superiority, though some think she really means those overseas, with the immigrant's burning ambition. Even that, however, is dubious. The head of an international school in Singapore feels that Ms Chua is describing a type of pushy middle-class parent-of any ethnicity-found across the world. He does not recognise a common caricature of multi-ethnic parent-teacher meetings: Western parents grumbling that little Joshua has so much homework he has had to cut back on other pursuits, including relaxing; Chinese parents complaining that they are having to send poor Mingming to bed before midnight because she runs out of homework.

He does, however, see a grain of truth in the notion that Asian mothers, more comfortable than Westerners with the idea of meritocracy, drive their children hard. The headmaster also thinks there is something in Ms Chua's argument that Chinese parents believe "their kids owe them everything", whereas Westerners think that the obligation lies all in the opposite direction.

Educational methods certainly do differ. Children coming into his school from the local system sometimes suffer exam-deprivation anxiety. Yet, despite the great success of its education system, Singapore has been reforming it to lay less stress on rote-learning and repetitive tests and more on self-expression.

In China itself great dissatisfaction exists with the quality of education, and a debate rages about discipline. The recent suicide of an 11-year-old boy struggling with a school punishment (copying pages from a book) provoked a revealing reaction. One blogger, as reported by chinaSMACK, a website, thought the incident showed that children these days are just too fragile. Another hoped the dead boy might be reincarnated in America, where "studying is relaxed and the homework load is light too."

The campaign to criticise Dr Spock and Confucius

In a month which saw a statue of Confucius unveiled near Tiananmen Square, few dispute that Chinese tradition has a tenacious grip. But for all his stress on filial piety, Mencius wanted children treated "with the kindness due to youth". Another website, the Useless Tree, which tracks "ancient Chinese thought in modern American life", puts Ms Chua not in the Confucian tradition but in the rival, harshly realist, "Legalist" school. Han Feizi, a Legalist thinker born about a century after Mencius, warned that "the children of a kindly mother often turn out bad." To Americans rattled by Ms

Chua's diatribe, it may be some consolation that, in China as in America, disagreement about how to raise children is as old as the country itself.

Economist.com/blogs/banyan

Correction: Nagasaki

Jan 20th 2011 | from PRINT EDITION

In our piece on Nagasaki last week, we should have said that the prefecture, not the city, had a population of 1.45m. Our apologies. This has been changed online.

Israeli politics

Can the doves take off again?

Jan 20th 2011 | *JERUSALEM* | from PRINT EDITION

A split in Israel's Labour party may give the peace-minded left a new lease of life

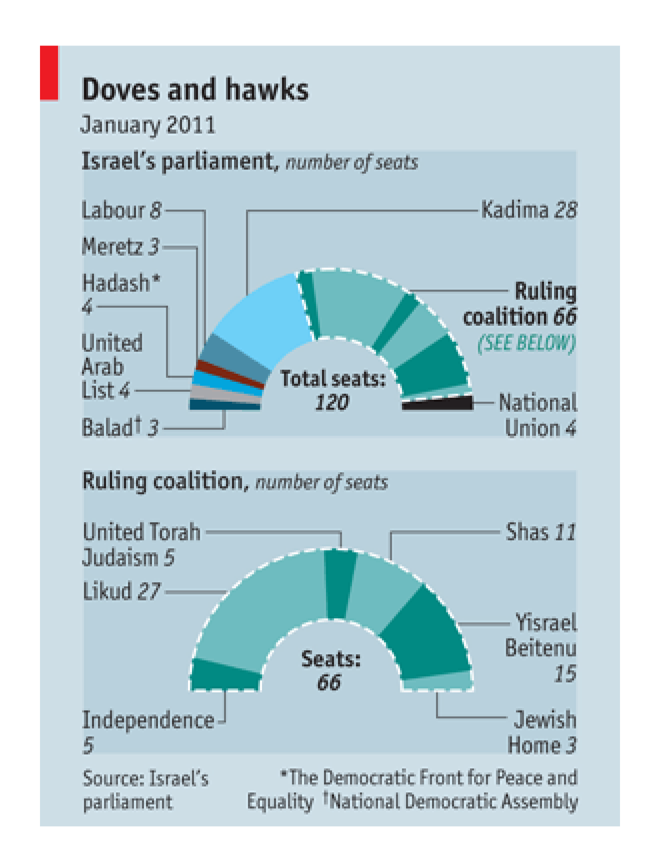


AFTER Binyamin Netanyahu's coalition recently shrank from 74 seats to 66 in Israel's 120-seat parliament, he insisted that his government had become stronger. Maybe so. But the opposition has got stronger too, as well as larger. Israelis who bank on peace through negotiation with the Palestinians may have a chance to revive.

The coalition shrinkage was caused by a split in the Labour party, always a restless partner. Labour's leader, Ehud Barak, the minister of defence, quit his party, together with four other members of parliament, setting up a new faction called "Independence". The reduced Labour party, now numbering just eight parliamentarians, has gone over to the opposition.

The shake-up, as Mr Netanyahu points out, makes his rightist-religious coalition more cohesive ideologically, and thus, he hopes, more disciplined politically. But by consolidating the hawks, the new alignment may also unify and perk up the doves in Israel's aviary. There is a rare flutter of excitement on Israel's left.

Mr Barak's move, excoriated by the Labour rump as opportunistic, is the latest in a series of mergers and secessions that has eroded the old pattern of Israeli politics. For decades a "national camp" comprising the Likud and its allies was pitted against a "peace camp" made up of Labour and like-minded parties, including Israeli-Arab parties. The religious parties were in the middle, inclined to the nationalists but always ready to negotiate with the peaceniks if the parliamentary arithmetic warranted it.



The most cataclysmic of those shifts was in 2005, when the then prime minister, Ariel Sharon, seceded from the Likud to create Kadima, now the largest party in parliament (see chart). This shift had been preceded in the late 1990s by the rise of two new parties: Shinui, an anti-clerical outfit founded by Tommy Lapid, and Yisrael Beitenu, a far-right party, backed mainly by Russian immigrants, led by Avigdor Lieberman. Shinui, a linchpin of Mr Sharon's governments between 2001 and 2006, has since disappeared as swiftly as it arose.

Israel's fluid and fickle party structure reflected a blurring of the old hawk-dove demarcation. The Likud, like Kadima and Labour, purported to support (or at least to acquiesce in) the view that the Israel-Palestine conflict can be solved by creating two sovereign states existing side by side. That was Mr Netanyahu's message to the world after he took office in 2009. His generous disbursement of ministries to Labour was meant to keep onside Mr Barak, a former prime minister in a doveish coalition from 2000-2001, lending credibility to his professed desire to negotiate peace.

But that credibility has been fizzling at home and abroad, since Mr Netanyahu refused to meet the minimal demand of his Palestinian interlocutors (and of Western mediators) that Israel should stop expanding Jewish settlements on the West Bank, the main bit of the Palestinians' would-be state. Labour's break-up may help reclarify the old hawk-dove ornithology. The evolving demarcation is between Israelis who still want, above all, to end the occupation of the Palestinian territories by negotiation or else by unilateral withdrawal, and those (now apparently including Mr Netanyahu) who prefer to stay put, for religious, nationalist or, as many more middle-of-the-road Israelis see it, security reasons.

Could a reconsolidated peace camp win back the middle-of-the-roaders? Tzipi Livni, Kadima's leader, has done well to hold her own ranks together, talking tough on security but consistently arguing for negotiation with the Palestinians. She may pull in some moderate Likud people unhappy with a series of bills before parliament that seem to discriminate against Israeli-Arabs and constrict freedoms. Mr Lieberman, the foreign minister, repulses many in the middle of Israel's spectrum with his verbal assaults on human-rights groups, accusing them of treachery.

Meanwhile there is speculation that a new secular centrist party may emerge before the next election, set for 2012 unless the government falls before then. A popular broadcaster, Yair Lapid, son of the late Shinui leader, is said to be mulling his

prospects. The guess is that he would rather align with Kadima than with the Likud. A regrouping of social democrats on Kadima's left flank, with Meretz and Labour to the fore, is also being mooted.

That is the hope of Isaac Herzog, minister of welfare until the recent split, who intends (among several others) to run for the Labour leadership. The scion of a patrician family-his uncle was Abba Eban, a longtime foreign minister, and his father, Chaim, was Israel's president-Mr Herzog says Labour must recover the social democratic values of the party's founding fathers. But would that provide the basis of a ruling coalition on the centre-left with the clout to cut a deal with the Palestinians? That remains a speculation too far.

Index | Middle East & Africa

Syria's economy

Hard choices for the government

Jan 20th 2011 | *DAMASCUS* | from PRINT EDITION

Will President Bashar Assad hold his nerve?



The market must prevail

SYRIA has been edging away from a centrally planned socialist economy to a "social market" one. "The last five years have been about deconstructing the socialist ideology in favour of the market," says an adviser to the government. "The next five will be about implementing it." That means big cuts in subsidies and painful belt-tightening for Syria's far-from-opulent masses. But will the government, seeing unrest simmer in the region in the wake of Tunisia's upheaval, hold its nerve?

The proposed changes risk breaking the social contract long upheld by President Bashar Assad's Baath party. The old deal meant low wages and secure jobs, while providing life's basics, such as food and fuel, very cheaply. The new plan envisages raising cash by issuing government bonds and soliciting foreign investment to the tune-it is hoped-of $55 billion. As subsidies shrink, the price of fuel, electricity, water, transport and food should rise to market levels.

Fearing unrest, the government recently wobbled. It announced a 72% rise in heating-oil benefits for public workers and froze the price of electricity. But it sorely needs more cash. Oil revenue has dipped as the population, which has doubled to 22m since the mid-1980s, continues to soar. The government cannot put off its reforms for long.

The IMF has for years been urging Syria to do away with subsidies. In 2008 the government leapt ahead of its counterparts in the region, notably Egypt, by raising petrol prices. It removed subsidies for fertiliser but kept many items, including electricity and food, artificially cheap. Direct energy subsidies still cost Syria around 5% of GDP a year, according to the government and the IMF.

Farming, a mainstay of the economy, is also being liberalised. An agricultural fund has been set up to replace blanket subsidies. The list of key crops, which have their prices set by the government as the sole buyer, has been pared down from seven a decade ago to three today: cotton, sugar beet and wheat-deemed the "red-line" crop since it is the basis for bread, the people's staple. But Syria's land is hard-pressed to meet demand, let alone provide for a strategic reserve.

The steady introduction of market reforms since 2005 has yet to make a big difference. Opening up business has so far benefited only a few. Property has been bought for speculation. Food prices have risen faster than wages. Quite a few industrialists have seen their businesses founder in the face of cheaper goods from China and Turkey. Plans to ease the pain by creating a welfare safety net have fallen behind. People scrimp to pay for private education and health care because state provision, due to be overhauled in the next five years, is so bad. "The growing wealth gap is threatening the middle class," says a local economist.

Elections due this year are sure to be tightly controlled. People are still too scared to protest. And events in Tunisia may make the government even warier about pushing ahead with its reforms.

Nigeria's presidential primary

Another term beckons

Jan 20th 2011 | *ABUJA* | from PRINT EDITION

To prove himself, the president needs to do more than win an election primary

IT TOOK President Goodluck Jonathan a mere decade to go from lowly official to undisputed leader of his country. He became president by default a year ago and has now clinched the nomination for presidential candidate in Nigeria's ruling People's Democratic Party (PDP) by winning 77% of the vote in a primary on January 14th. He is now the favourite to triumph at a poll due in April. Yet many still think his best quality is a knack for being in the right place at the right time.

Having long laughed at his seemingly apt name, Nigerians are far from certain what lies ahead. Africa's most populous country and biggest energy producer, Nigeria is the continent's giant, with 150m people, over 250 ethnic groups and at least 36 billion barrels of proven oil reserves. Yet it is also known for a level of chaos and corruption that makes other Africans raise their eyebrows at the mention of its name. A string of military and civilian leaders have embezzled the country's oil wealth rather than investing in basic infrastructure. The chasm between rich and poor fuels militant gangs in the oil-rich southern delta and Islamist sects in the arid north.

Mr Jonathan vowed to halt decades of misrule on becoming a stopgap president last May. He was ushered in to fill a vacuum on the death of the then president, Umaru Yar'Adua, whom he had served as deputy. Just a few years earlier, he had likewise been drafted in to replace a state governor impeached on graft charges. On taking the top job, he promised to solve three of the country's biggest problems: rigged elections, a woeful electricity supply and the militancy in the delta, whence he hails. He later added that he would run in the next elections.

Mr Jonathan has made the right noises on the state-run power sector. He has put forward a privatisation plan that aims to raise $35 billion of investment over the next decade and stipulates that private companies put tens of billions of dollars into areas such as electricity transmission. Today's grid cannot generate enough electricity even to power a 40-watt bulb around the clock for every Nigerian-and rarely runs at full capacity. "If he can just sort out power, then that is enough for us," said one delegate at the primaries. Foreign investors are interested but only the boldest will invest before the election.

Mr Jonathan also has much to do to clean up elections. He has appointed Attahiru Jega, a respected academic, to head the election commission. Mr Jega has focused most of his energy on compiling a voters' register at a cost of $580m, complete with fingerprints and photographs. A bogus list containing celebrities' names was central to rigging the last polls, in 2007. Voter registration began on January 15th and is lurching ahead, despite delays and faulty equipment.

The PDP has relied on force and fraud to win all three elections since army rule ended in 1999. A reliable voters' list alone does not prevent foul play. Local politicians may still intimidate or pay off voters; local election-officers may still fiddle results after votes are in. "There are still gaps that the commission needs to address, but their excuse is they do not have as much time as there needs to be," warns Clement Nwankwo, a campaigner for democracy and a consultant on electoral reform.

Mr Jonathan's record on security is less impressive. He has just about maintained an amnesty for delta militants who were blowing up foreign oil companies' pipelines and kidnapping their staff. The violence remains far below its peak of 2008 and production has stayed above the acceptable mark of 2m barrels a day. But new militant bosses started appearing late last year, replacing those bought off under the peace deal. Mr Jonathan's candidacy, which breaks a PDP pact under which the presidency rotates between the mostly Muslim north and largely Christian south, could also stir up northern youths.

But the main worry is the president's spending. With crude prices touching $100 a barrel, Nigeria's piggy bank, the so-called "excess crude account" for surplus oil revenues, should be bursting. Instead, it has been drained from $20 billion in 2007 to $300m this year. The president handed out another $1 billion from the savings to government officials at Christmas.

"The spending has been substantial but there is nothing to show for it," says Bismarck Rewane, a financial analyst in Lagos, Nigeria's business capital. Few infrastructure projects warranting such spending are under way, he adds. Many conclude that the "accidental president" has had to relax controls to win over Nigeria's political elite. Tales abound of both Mr Jonathan and Atiku Abubakar, his northern challenger, wooing delegates for months before the primaries with promises of cash and political appointments.

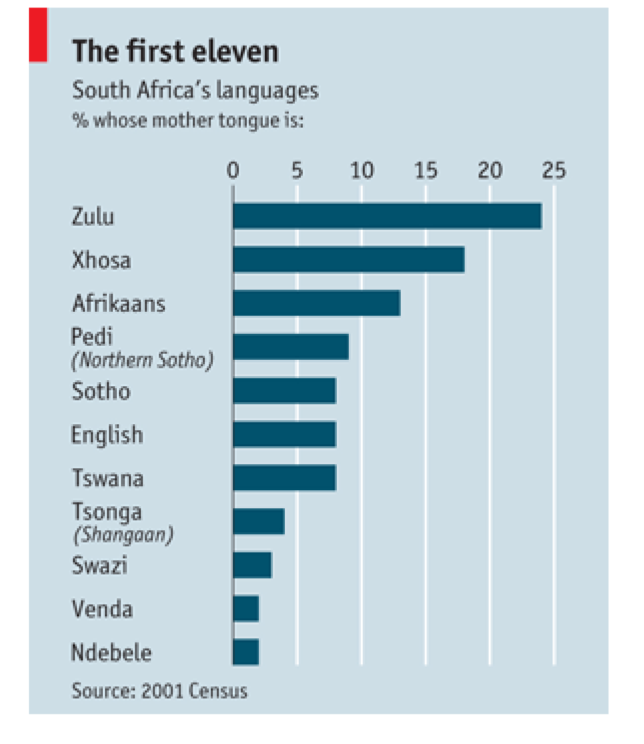
Mr Jonathan's backers say he will come into his own if he gets a proper mandate in April, breaking free of those he now has to woo. Until then, his true colours remain hard to ascertain. "Once he gets in, that will be the real test of leadership," says Mr Rewane. "Is he strong enough to tell those cronies that the party's over?"

South Africa's languages

Tongues under threat

Jan 20th 2011 | *JOHANNESBURG* | from PRINT EDITION

English is dangerously dominant



UNDER the 1996 constitution, all 11 of South Africa's official languages "must enjoy parity of esteem and be treated equitably". In practice English, the mother tongue of just 8% of the people, increasingly dominates all the others. Its hegemony may even threaten the long-term survival of the country's African languages, spoken as the mother tongue of 80% of South Africans, despite the government's repeated promises to promote and protect indigenous languages and culture.

Under apartheid, there were just two official languages, English and Afrikaans, a variant of Dutch with a dash of French, German, Khoisan (spoken by so-called Bushmen and Hottentots), Malay and Portuguese. Pre-colonial African languages were relegated to the black townships and tribal "homelands". Even there, English was often chosen as the medium of education in preference to the inhabitants' mother tongues. Black South Africans increasingly rejected Afrikaans as the language of the main oppressor; English was a symbol of advancement and prestige.

Today, 16 years after the advent of black-majority rule, English reigns supreme. Not only is it the medium of business, finance, science and the internet, but also of government, education, broadcasting, the press, advertising, street signs, consumer products and the music industry. For such things Afrikaans is also occasionally used, especially in the Western Cape province, but almost never an African tongue. The country's Zulu-speaking president, Jacob Zuma, makes all his speeches in English. Parliamentary debates are in English. Even the instructions on bottles of prescription drugs come only in English or Afrikaans.

Yet most black South Africans are not proficient in English. This is because most of their teachers give lessons in a language that is not their own. To give non-English-speaking children a leg-up, the government agreed last year that all pupils should be taught in their mother tongue for at least the first three years of primary school. But outside the rural areas, where one indigenous language prevails, this is neither financially nor logistically feasible.

Some people suggest reducing the number of official languages to a more manageable three: English, Afrikaans and Zulu, the mother tongue of nearly a quarter of South Africans. But non-Zulus would object. Unless brought up on a farm, few whites speak an African language. For the school-leaving exam, proficiency in at least two languages is required. But most native English-speakers opt for Afrikaans, said to be easy to learn, rather than a useful but harder African tongue. At universities African-language departments are closing.

Some effort is being made to protect African languages from this apparently inexorable decline. The *Sunday Times*, South Africa's biggest-selling weekend paper, recently launched a Zulu edition. In September the Oxford University Press brought out the first isiZulu-English dictionary in more than 40 years.

Many of the black elite, who send their children to English-speaking private schools or former white state schools, may accept English emerging as the sole national language. Many talk English to their children at home. Fluency in the language of Shakespeare is regarded as a sign of modernity, sophistication and power.

Will South Africa's black languages suffer the fate of the six languages brought by the country's first Indian settlers 150 years ago? Maybe so, thinks Rajend Mesthrie at the University of Cape Town. For the first 100-odd years, he says, South

Africa's Indians taught and spoke to their children in their native tongues. But English is now increasingly seen as "the best way forward". Today most young Indians speak only English or are bilingual in English and Afrikaans, though they may continue to chat at home in a kind of pidgin English larded with Indian and Zulu.

Spain and the euro crisis

A great burden for Zapatero to bear

Jan 20th 2011 | *MADRID* | from PRINT EDITION

The Spanish prime minister has become a reluctant convert to reform-but maybe too little, too late



THE Madrid metro station of Pitis sits in an urban wasteland, a shiny monument to Spain's housing collapse. Nobody ever came to build the apartment blocks that the station was meant to serve. Roads, pavements and streetlamps were all laid out-but then the property bubble burst. In a country with 700,000 unsold new homes, building-land right across Spain has plunged in value.

Pitis's echoing, empty station is witness to Spain's gloom. It is also concrete proof that Jose Luis Rodriguez Zapatero, the Spanish prime minister, was wrong to blame the country's tumble into recession and its 20% unemployment solely on a global credit crunch generated on the other side of the Atlantic. Spain created many of its own problems-toxic loans on building-land are just the start. These shortcomings have been ruthlessly laid bare by the euro crisis. Has Mr Zapatero seen the light?

Judged by his recent words, it seems that he has. The prime minister proclaims a new-found reforming zeal. "There is something worse than the lack of a broad consensus about how to implement reforms and that is, especially at this moment in time, a lack of reform," he said earlier this month.



He promises to reform pensions by January 28th and collective bargaining by March 18th. New transparency rules for banks, to clarify exposures to bad loans against building-land or unsold property, are in place. The same goes for regional governments, which account for a larger share of public spending in Spain than in other countries (see chart), and are now being asked to control their own deficits. Unions, employers and government have begun frantic talks to see if they can agree on more reforms to collective bargaining. Some hopeful analysts believe that Spain, which returned to (albeit very low) growth in 2010, is finally turning the corner.

Mr Zapatero's new-found confidence and readiness to embrace reform has several causes. A deal with the Basque Nationalist Party (PNV) means that his minority government should survive until the election due in early 2012. The promotion of the interior minister, Alfredo Perez Rubalcaba, in October has given him an able, popular and hyperactive deputy prime minister. Mr Zapatero may choose not to stand again for prime minister, so he has little left to lose. Mr Rubalcaba looks an increasingly obvious successor as leader of the Spanish Socialist party.

Yet Spain's road to recovery is still fraught with dangers. The fall in house prices (of just 13.1% from the peak) surely has further to go. The burst bubble has exposed more than Spain's addiction to construction, which at its height accounted for 13% of jobs. It has also exposed the economy's waning competitiveness. According to a study by FEDEA-McKinsey, a consultancy, Spanish competitiveness deteriorated by 33% against Germany in the ten years to 2009. Membership of the euro precludes correcting this by devaluation. Mr Zapatero's conversion to reform may be genuine, but it comes late and may not go far enough. It is not clear that he accepts the case for wage cuts, for example.



The need for reform and austerity is urgent. As Portugal teeters on the verge of a bail-out, Spain yo-yos anxiously. It has just had to pay a steep 5.5% on a euro6 billion ($8 billion) syndicated bond. Spain's fellow euro members are looking for broader solutions to their sovereign-debt crisis, in which Spain (by virtue of its size) is by far the biggest risk. Mr Zapatero's government wants them to do more (eg, by approving the issuing of euro bonds) but, for now, the Spanish must look after themselves.

Elena Salgado, the finance minister, trimmed the budget deficit from 11.1% of GDP in 2009 to under 9.3% in 2010. She aims to get it to 6% this year. Spain's national debt is below the euro-zone average and less than America's and Britain's. But, besides worries about hidden bad loans held by savings banks, investors see lack of growth as the main problem. A possible trap lurks: to regain meaningful growth Spain needs bigger reform, but austerity will also crimp growth.

Changes to pensions, at least, look safe. Mr Zapatero's deadline has concentrated minds. The retirement age will, with exceptions, rise from 65 to 67. But more labour reform is needed. He has given unions and employers until March 18th to

agree upon changes in the inflexible, top-heavy collective-bargaining system. This produced wage deals outstripping inflation in 2009, though the current level is well below inflation. The government must also complete last June's modest labour reform by defining how companies facing losses might shed workers. There are worrying signs that in refining the details, the terms for such actions may be made tighter than had been hoped.

Yet the unions are scared. Mr Zapatero showed in June that he could act without them. He sailed through a tepid September general strike. Now the unions and government want a grand pact, including employers and opposition parties, to back reforms. The employers have shown willing. The unions still hope to water things down. "My fear is that with the pact he will sell this reform out," says Luis Garicano of the London School of Economics.

The government has dragged its feet on reform in the past. A so-called sustainable economy law, which Mr Zapatero announced in May 2009, is still stuck in parliament. Mr Zapatero first mooted retirement at 67 last January. But he now looks more determined. If he can co-opt unions and employers, reforms should get easier. Germany, which maintained employment when its economy shrank in 2009 and then grew by 3.6% last year, is seen as an example to follow. Wage rises there were the lowest in the European Union over the past decade. A February visit by Chancellor Angela Merkel will be used to drive this message home.

Mr Zapatero is also trying to save his party, which trails the conservative People's Party (PP) by 15 points in opinion polls and is expected to do badly in May's local elections. Quick reform could give the Socialists time to recover by 2012. "The time for time-wasting is over," says the PP's leader, Mariano Rajoy. Will he sign up to a national pact? He has preferred to let the government suffer the unpopularity of reform alone. But Mr Zapatero does not have to wait for him-or for the unions. He has a golden opportunity to act boldly now.

Index | Europe

France and Africa

Ties across the Mediterranean

Jan 20th 2011 | *PARIS* | from PRINT EDITION

A principle of non-interference that is not always applied in practice



The best of friends-before the jasmine revolution

CAUGHT napping by the "jasmine revolution" in Tunisia, France's government did what the French do best: worked up a theory to explain itself. France was not only a step behind events but, unlike America, failed to condemn the regime's

violent response to protesters. And days before the flight of Zine el-Abidine Ben Ali, the Tunisian president, Michele Alliot-Marie, the foreign minister, clumsily offered the "savoir faire" of France's security forces to its former protectorate, albeit to avoid endangering protesters' lives.

The doctrine that explains all this, the government said this week, is "the principle of non-interference". For decades after its African possessions won independence, French officials, oil bosses and soldiers meddled behind the scenes, propping up many unsavoury leaders along the way. A web of contacts known as *francafrique* linked African leaders and petrodollars to French political parties and presidents from left and right. When he was elected president in 2007 Nicolas Sarkozy promised to sweep away these "networks of a bygone era" and to replace them with grown-up, bilateral ties free of post-colonial paternalism.

In some ways France has turned a page. Mr Sarkozy has opened a new military base in Abu Dhabi, where France has no colonial link, and handed back to Senegal one of three permanent bases in Africa (those in Gabon and Djibouti remain). He has updated opaque bilateral defence accords. He has courted leaders outside the French-speaking backyard. Since Osama bin Laden declared France a terrorist target after its ban on the burqa, Mr Sarkozy has focused particularly on counter-terrorism.

But does France's new approach really amount to non-interference? "France used to intervene in order to exist internationally," comments Dominique Moisi, of the French Institute of International Relations. "We are witnessing a reversal of this attitude, but it is taking place in a chaotic, if not contradictory, manner." As Mr Sarkozy conceded this week, the principle of non-interference sometimes clashes with another underlying principle that he claims for French diplomacy, which is to support freedom and democracy.

Consider recent events in three former French territories: Cote d'Ivoire, Tunisia and Niger. When Laurent Gbagbo refused to resign as president of Cote d'Ivoire after losing an election, Mr Sarkozy ordered him to go or to face sanctions. This was in tune with the international consensus, but it was nonetheless perceived as imperious. "Cote d'Ivoire is not a sub-prefecture of France," snapped one Ivorian minister. Mr Sarkozy's ultimatum has now expired, with no effect. France has hundreds of soldiers in the country in a peacekeeping operation, who were sucked into a bloody stand-off a few years ago. Nobody wants that again. But would France stand on the sidelines were the African Union, now mediating in the stalemate, to urge the use of force to dislodge Mr Gbagbo?

If the French are unavoidably involved in Cote d'Ivoire, they have been denounced at home for doing nothing in Tunisia. "Scandalous", "shameful" and "ignoble" were some of the more printable adjectives lobbed this week by the opposition Socialist Party (which, when in power, was just as cosy with the Ben Ali regime). The French blogosphere has dug up evidence of Franco-Tunisian complicity for Facebook's "Ben Ali Wall of Shame". When Mr Sarkozy and his wife, Carla Bruni, went on a state visit in 2008, the president announced that Tunisia's "space of freedom is progressing."

In reality, France was no more supportive of the Tunisian regime than many others who saw it as a bulwark against Islamism. But its ties to the country are more complex than most. At least 600,000 Tunisians live in France, including many political exiles. France is Tunisia's biggest trading partner. Several French politicians were born or have homes in Tunisia. This mesh of intimate ties also explains France's confusion. Having been slow to speak out, it was quick to refuse the fleeing president sanctuary on French soil.

A third, quite different, case concerns the recent kidnapping and execution of two young Frenchmen snatched in a restaurant in Niger by gunmen acting for al-Qaeda in the Islamic Maghreb (AQIM). As Niger's army chased the kidnappers across the desert, French special forces were called in and carried out an assault by helicopter. Several AQIM gunmen were killed in the shoot-out. Elsewhere in the Sahel, five French hostages are still being held. AQIM killed another last year.

Plainly, fighting terrorism or hostage-taking in the Sahel is a different sort of intervention. But it also reflects how France is trying to redefine its role in Africa. Last year Mr Sarkozy said it was "not a strategy" for France to pay ransoms to kidnappers in the Sahel, or even to negotiate with them. Instead, it would aid any country requesting help to hunt down AQIM. "This was a major strategic change," says Francois Heisbourg of the Foundation for Strategic Research. The special forces that France has stationed in the Sahel explain how the Niger kidnappers were tracked so rapidly. In short, France may want neat principles for its new diplomacy in Africa; but the reality is a lot more blurred.

A party animal

Jan 20th 2011 | *ROME* | from PRINT EDITION

Why the prime minister may yet survive his latest sordid sex scandals



Too many late nights?

CETTO LA QUALUNQUE is an irredeemably corrupt, vulgar businessman from Calabria, Italy's mobster-ridden toe. He has just returned from a stretch on the run from the law to stand for mayor of his native, bullet-ridden Marina di Sopra (ominously twinned with Weimar). Unlike Martin Luther King, he says, "I have no dream...but I do like *pilu* [a dialect term for a bit of tail]." Mr La Qualunque, the central character in a new film, "Qualunquemente", is an invention. But this week he suddenly looked awfully real.

On January 17th Milan prosecutors submitted to parliament a dossier of statements, reports and wiretap transcripts that depicted scenes as extravagantly sordid as anything in the much-trailed comedy. They included orgiastic parties staged at the home of Italy's prime minister, Silvio Berlusconi, involving more than 20 half-naked women, and a room for what are known to participants as "Bunga Bunga" sessions, equipped for pole-dancing, with wardrobes full of skimpy nurses' and policewomen's uniforms.

The dossier summarised an inquiry that represents perhaps the biggest threat so far to Mr Berlusconi and his three-year-old conservative government. On January 14th the prime minister learnt that he had been placed formally under investigation, suspected of two offences: paying for sex with an underage prostitute and abusing his position by trying to cover it up. The alleged prostitute is a Moroccan runaway, Karima el-Mahroug (known as Ruby). The dossier, sent to Rome because investigators need parliamentary consent for a crucial office search, claims that Ms el-Mahroug visited Mr Berlusconi's villa near Milan eight times in 2010. When she was taken to a police station on suspicion of theft in May, she was handed over to an associate of the prime minister after a call from his office. The prosecutors believe they have enough proof to have Mr Berlusconi indicted without a pre-trial hearing. He could even be in the dock by May.

The solution to this crisis that might suggest itself in most other countries was flatly ruled out by the prime minister on January 18th. "Resign?" he asked journalists. "Are you mad?" Once again, he seems bent on facing down claims that would persuade most normal public figures that the time had come for retirement, perhaps to a monastery. This is the

seventh sex scandal in which Mr Berlusconi has been personally implicated. But as the others have shown, the mechanisms that drive out politicians elsewhere do not really apply in Italy, or at least not to Mr Berlusconi.

Most political leaders in other countries are persuaded to go before any charges reach the courts by their own followers "for the good of the party". But since the electoral law introduced by Mr Berlusconi's previous government in 2005 makes Italian parliamentarians dependent for re-election entirely on their party leaders, who decide where to place candidates on the party lists, such rebellions are almost impossible to organise. This is especially true in the prime minister's People of Freedom (PdL) movement, many of whose parliamentarians owe their political careers to Mr Berlusconi.

After surviving two opposition no-confidence motions last year, the prime minister's main apparent vulnerability is to desertion by the PdL's allies in the Northern League. So far, they have remained loyal, even though part of the league's original mission was to clean up public life. But the government is now so hamstrung that it may be unable to secure the tax reforms that the Northern League's leader, Umberto Bossi, touts as the price of continued support. Unless he withdraws that support, the only route that could topple the prime minister would seem to run through the courts. And that is a potentially winding path, punctuated by side-turnings down which Mr Berlusconi could easily escape again.

For a start, his lawyers argue that the Milan prosecutors have no right to investigate the alleged offences, since Mr Berlusconi's villa lies outside the city's judicial boundaries (as does the home of the police official who took the late-night call from his office that led to Ms el-Mahroug's release). They will also note that Mr Berlusconi and his young friend have both denied having sex and say there is no conclusive proof that they did, let alone that he paid for it. Accounts of the "Bunga Bunga" sessions include much alleged lewdness, but no mention of actual sex.

The accusation that the prime minister abused his powers may be easier to prove and carries a heavier maximum sentence (12 years against three for having sex with a juvenile prostitute). But Mr Berlusconi's lawyers could protest that such a charge requires trial by a special court and approval by the Chamber of Deputies.

There are two big dangers in this uncertain situation. One is that the government, which has been unable to do much for the past two years because its leader has been repeatedly distracted by problems of his own making, remains inert for months to come, heedless of Italy's economic problems. The second, perhaps greater, risk, which was suggested by Mr Berlusconi this week, is that he may seek a new mandate to crush the independence of the judiciary in an election that might threaten the very foundations of his 150-year-old country. Poor Italy.

Index | Europe

Lithuania and Poland

Bad blood

Jan 20th 2011 | *VILNIUS* | from PRINT EDITION

Lithuania and Poland seem to have hit an icy impasse



POLAND was one of Lithuania's best friends in January 1991. As Soviet troops tried to impose a puppet regime in Vilnius, Lithuania's foreign minister, Algirdas Saudargas, fled to Warsaw, ready to head a government-in-exile if the worst happened. Polish politicians condemned the Soviet crackdown. It failed, but 14 unarmed protesters were shot and crushed by tanks, with hundreds maimed or injured.

Twenty years on, at ceremonies to commemorate these events, Poland was represented by only a low-level delegation, announced at insultingly short notice. Poland's patience is at an end, says a senior diplomat, citing Lithuanian foot-dragging on restitution of pre-war Polish property, broken promises on language rights for the ethnic Polish minority, attempts to undermine its schools and ill-treatment of a Polish-owned oil refinery.

Lithuanians are incensed and feel bullied by their bigger neighbour. Lithuania is the only country outside Poland to offer Polish-language education from infancy to adulthood, they point out. Latvia's arrangements for its Polish minority are broadly similar. Ethnic Lithuanians in Poland have problems, too. So why the fuss?

Some think the thaw in relations between Warsaw and Moscow has sparked mischief-making. Others suggest that Radek Sikorski, Poland's foreign minister, has a personal vendetta against Lithuania (he insists he does not). But personalities do play a role. Lithuania's president, Dalia Grybauskaite, was to blame for a spectacularly stormy meeting last year with Bronislaw Komorowski, her Polish counterpart, say outsiders who were there.

The two prime ministers, Audrius Kubilius of Lithuania and Donald Tusk of Poland, get on fine, unlike their combative foreign ministers. One reason may be that Mr Tusk is a member of Poland's small Kashubian minority and thus more sensitive to the worries that small ethnic groups have about big ones.

Plenty of people think the row has gone too far. Polish newspapers criticised the decision to snub the Lithuanian anniversary ceremonies. America wants both countries to co-operate more, not least in regional military exercises planned for this year and next. Estonians and Latvians fear the dispute may block better road, rail and power links to the south-east that will end their isolation from the rest of Europe.

The real problem lies in differing interpretations of history. Each country insists that the other behaved badly in the past but skates over its own mistakes. After Polish troops seized Vilnius (then called Wilno) in 1920, the pair spent the inter-war years in a stony fury. That ended in disaster for both. Some worry that this sorry history may repeat itself. Yet the blunt truth is that Poland can afford to ignore Lithuania, whereas Lithuania and its Baltic friends cannot do without Poland.

Index | Europe

Teaching German immigrants history

The past is another country

Jan 20th 2011 | *BERLIN* | from PRINT EDITION

Muslim immigrants learn about Germany's Nazi past

BERLIN'S Holocaust memorial is a short hop from Neukolln, yet is in a different world. The memorial's undulating concrete blocks are a sombre oasis in the city centre. Neukolln is home to immigrants and poor students. But Djamila Boumekik, who came to Germany from Algeria 20 years ago, knows the memorial well. "In Algeria no one talked about Nazism. Here you have to learn this history," she says. For Mrs Boumekik is an alumna of "neighbourhood mothers on the trail of history", a 60-hour tutorial about the Nazis designed for immigrant women who also act as social workers.

The initiative came from the women, says Jutta Weduwen of Aktion Suhnezeichen Friedensdienste, which runs the seminars. They stumble across the history in schools or debates on Israel and want to know more. About 100 women from Berlin and Cologne have attended seminars, which include meeting Holocaust survivors and visiting concentration camps. The idea, says Mrs Weduwen, is to deepen participation in German life. But it is fraught with peril. A sense of national responsibility for the Holocaust is part of German identity. Yet the idea that a woman in a headscarf could have any interest in it provokes disbelief. "You're just an immigrant. You have nothing to do with this," said a group of German

women to Mrs Boumekik. The interior ministry, which provides part of the money, may be as keen to discourage Islamist extremism and anti-Semitism as to promote participation.

The unspoken assumption is that there is a middle ground between German remorse and indifference. As enlightened Germans, the seminar-givers see the Holocaust as a unique crime committed mainly against the Jews. Yet they must make room for the views of women whose backgrounds have little to do with the persecution of Jews and who may have suffered horrors of their own. Taking their experiences seriously matters as much as instructing them. There is a risk of "relativising" the Holocaust, says Astrid Messerschmidt of the University of Education in Karlsruhe. Yet the German version of history "cannot be imposed from above".

Most fraught, says Mrs Weduwen, are discussions of the Middle East. The women learn that both sides in the Israel-Palestine conflict have grievances. The message can receive a hostile reception when Israeli commandos storm ships trying to break the Gaza blockade. Mrs Boumekik is involved in educating Arab families who blame Jews for the conflict. That is like assuming Muslims are terrorists, she says. With hostility to Muslims mounting in Germany, some women draw parallels with Nazi racism. Mrs Weduwen may drop the camp visits, which sharpen such fears. "This shouldn't be shock pedagogy," she says.

Index | Europe

Charlemagne

The name's Bond. Eurobond

Jan 20th 2011 | from PRINT EDITION

The European Union finds an unexpected new hero in the financial markets



IN EUROPE over the past year, Bond has been the villain rather than the hero. Licensed to kill national economies, he brought down first Greece and then Ireland. Portugal and others are now cowering in fear. This Bond, it seems, is the agent of sinister Anglo-Saxon market forces seeking to destroy Europe's single currency. Such is the story most commonly told since the start of the euro zone's sovereign-debt crisis.

Of late, though, the villain has been partially rehabilitated. For the new Bond is now said to be a European federalist in disguise. As Jose Manuel Barroso, president of the European Commission, has claimed, "the markets are sending every day a very clear message that Europe has to work in a more co-ordinated manner when it comes to economic and financial issues." Jean-Claude Juncker, president of the euro group of finance ministers, insists that the euro zone has "the

confidence of the market". The proof, he says, was the strong demand for the commission's first issue of bonds this month to raise money for Ireland's bail-out, at an interest rate of only 2.6%.

Does the new Bond really want "more Europe"? Talk to market participants and the surprising answer is often yes. This is not out of love for the European dream, but rather out of fear of catastrophic losses. More decisive action is needed by the solvent north European countries, they are saying, to stop the crisis spreading right across the southern belt.

After the launch of the euro in 1999 the bond markets were quick to shake off their doubts about the durability of monetary union without a common fiscal or economic policy. The risk of devaluation was gone and the chance of default seemed tiny, to judge from the markets' judgment that bonds issued by thrifty states were barely worth any more than those of profligate ones. It was only late in the global crisis, when Greece admitted to lying about its numbers, that the markets woke up from their torpor into a sudden panic over sovereign risk.

Governments responded first by signing over vast emergency loans to Greece and then by creating an even vaster temporary loan facility (partly using IMF money). They drew on this for Ireland's recent rescue. The temporary will now become permanent, requiring a change to the EU treaties, with a new system under which the euro zone can in future restructure the debts of insolvent countries that share the currency.

The commission is seeking to bolster what it calls "economic governance": tougher monitoring of the budgets and economic policies of euro members, with the authority to issue warnings and even impose penalties against those (including surplus countries) that do not comply with Brussels's prescriptions. The EU is now embarked on its "European semester": the early submission of national budget plans and reform programmes to Brussels for scrutiny and peer review before they go before national parliaments. There is vague talk of deeper co-ordination. The Germans have spoken of setting a common retirement age across the EU; the French want more tax harmonisation.

All this goes far beyond what EU officials thought possible a year ago. Among other things, it will make Eurosceptic countries, notably Britain, far less likely ever to join the single currency. But will European governance assuage the bond markets? It has not so far. The markets' view, as far as anyone can tell, is that the EU bail-out funds must be expanded to remove any doubt about their capacity to save Portugal and Spain. Joint Eurobonds for part of the sovereign debt, called for by Mr Juncker and the Italian finance minister, Giulio Tremonti, might also reassure the markets. Above all, the markets want to see more common purpose from bickering European leaders.

Their political dispute centres on two questions. First, are the most solvent states, above all Germany, prepared to stand behind and if need be to subsidise the less solvent ones? Second, are the most indebted countries ready to endure economic pain-wage cuts, the end of cherished benefits and the imposition of labour-market reforms-to balance the books and encourage growth? The more convincingly the answer "Yes" applies to both questions, the faster calm will be restored. But so far the response has been slow, hesitant and contradictory.

Successful recent sales of bonds by Portugal, Spain and Italy have provided some relief. Germany says the EU should now seek an all-embracing deal, including on the size and scope of the bail-out fund, in time for the next summit in March. The commission retorts that the euro zone does not have the luxury of time: the markets have been "doped" by the opaque bond-buying by the European Central Bank (ECB), and probably by China and Japan, and need a clearer signal of action.

North is north and south is south

Do not expect the panic to be over soon. Northerners do not want to pay for the mess made by southerners. The olive belt cannot conceive of the harsh and unprotesting adjustment that Baltic countries have endured (with Estonia then leading the way into the euro). Many countries need years of austerity and reforms to regain lost competitiveness. Greater co-ordination and exhortation may help. But Mr Barroso and Mr Juncker and their promise of more European governance ultimately lack the persuasive power of the bond markets. Indeed, their plans will work only if markets remain alert, ready to jump on any hints of backsliding.

Calls for much greater "solidarity" from rich countries should therefore be treated warily, as should any suggestions that Brussels ought to seek to disarm markets by restricting derivatives trading or short-selling. The new Bond could turn out to be Europe's best friend in the end-but only if he is able to keep governments in fear for their lives.

Economist.com/blogs/charlemagne

Reforming public services

Where Thatcher feared to tread

Jan 20th 2011 | from PRINT EDITION

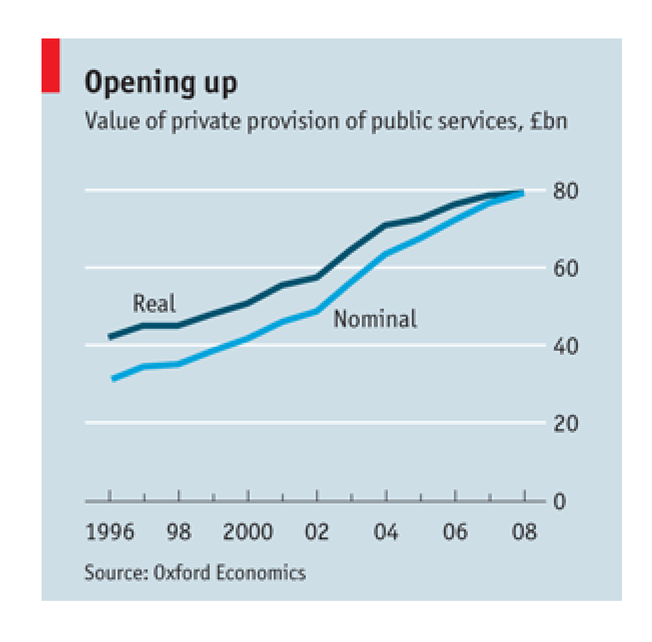
The coalition government is opening up the public services to competition and private providers to a much greater extent than any of its predecessors



Alamy/Bloomberg/reportdigital.co.uk/Paul Box

AN EARLY and important exchange of fire took place this week in the battle to reform the British state. Health-care managers, doctors' associations and the Labour Party attacked the coalition's plans to put family doctors in charge of commissioning hospital care for patients-including from private health-care companies, who might be able to offer some services at a lower price than the local hospital. As the government's health bill arrived in Parliament, David Cameron insisted that there is "no option of just quietly standing still".

However fierce the attacks, the direction of the caravan is clear. Across much of the public sector-from health and education to local authorities and prisoner rehabilitation-the provision of public services is increasingly being farmed out to private suppliers. The political risks are equally stark. The old slogan of the Thatcher-era ideologues-"Roll back the state"-has been decommissioned as too bracing, but a quiet and inevitably controversial revolution is under way.



Mr Cameron and Nick Clegg, the Liberal Democrat deputy prime minister, are accelerating and deepening Tony Blair's drive to increase choice and competition in the public services (see chart). They believe the evidence is on their side. A report commissioned by the previous government from DeAnne Julius, an economist, in 2008 concluded that the emergence of a "public service industry", distinct from state providers, had "made a major contribution to the provision of better value for money". She estimated the savings at "between 10% and 30% with no adverse effect, and sometimes an improvement, in service quality".

What the government now proposes goes farther and faster than previous efforts. Health reform is in the vanguard. The changes might seem unsurprising to other Europeans, many of whom have long had insurance-based health systems that feature competing providers. But the sacred status of the NHS-in which care is not only funded by the state but still overwhelmingly provided in publicly run hospitals-guarantees a backlash. Nigel Edwards of the NHS Confederation, which represents health-care managers, has predicted that by 2014 the NHS will look less like a single organisation than a "regulated industry".

If sensitivity to market-based reform is particularly acute when it comes to the health service, in some other areas it has gradually become a fact of life. Local councils of all political colours now contract-out important services. A report by Deloitte, a consultancy, points out that over 40% of local authority spending now goes to private providers, a figure set to rise after the passage of the government's localism bill, which is intended to devolve more powers from Whitehall to councils. Some cash-strapped local authorities are being more radical still: Suffolk, a Conservative fief in the east of England, is handing over a majority of its services, from libraries to children's facilities, to the private sector.

But there is potential for strife in areas besides the NHS. In education, the government wants to go farther than Mr Blair in challenging the dominance of comprehensive schools. It wants to see more academies, a form of semi-autonomous secondary school, often sponsored by private institutions and businesses. Meanwhile, one of the coalition's first acts was to declare that it was going to increase the participation of private and voluntary outfits in the training and resettlement of offenders: a mix of the compassion of the "Big Society", Mr Cameron's pet philosophy, and old-fashioned faith in the free market.

One problem for the government is that voters have been little prepared for such big changes. Margaret Thatcher's ideologues trumpeted devotion to the market-her ministerial ally, Nicholas Ridley, coined the "Selsdon Manifesto", explicitly recommending that the state retreat from delivering services, long before she took office. Today's Tories have tended to tread more softly, keen to lose their reputation as ideological state-slashers. Voters were reassured by Mr Cameron's pre-election avowals that the NHS was his priority-which fell short of saying that he intended to completely change how it runs. Even now, Andrew Lansley, the health secretary, is at pains to portray his plans as evolutionary rather than revolutionary.

Another difficulty is that adverse side-effects might well dominate the political debate before the benefits are felt, let alone appreciated by the public. The first symptoms of change will not be positive: the health reform and others will contribute to the imminent wave of redundancies in the public sector. Changes to more market-led provision on this scale also carry the risk of failures and uneven outcomes. The opposition is already claiming that the reforms reflect a callous ideological zeal.

And a fair amount of reform to date has entailed what one former cabinet minister calls "playing shops": there was no real risk of large institutions closing; failures were softened by state intervention. So when British Energy (now sold to EDF, a French energy group) faced financial difficulties in 2002, the Labour government committed over pound3 billion ($5.5 billion) to bail it out, so fearful was it of an energy shortfall and any perception of crisis.

The new breed of reformers might face similar regulatory dilemmas in more emotive policy areas. Market reforms involve stronger institutions taking over weaker ones. Yet even when some state schools are performing poorly, local parents often campaign against them being taken over, because they prize convenience and continuity over performance. In the event of big failures by a doctors' consortium or a hospital's management, the government's hope that accountability for outcomes will be devolved along with administration would be sorely tested. Patients put up with organisational shifts. They may be less understanding if a local health-care provider stops offering a service simply because it can no longer make money from it.

The history of reform since the 1980s shows that the public and professionals are often more flexible than instant cries of outrage suggest. The early rows over "contracting out" in the 1980s have subsided: the benefits of competition in areas from telecoms to utilities are now widely accepted. But only after a fight. Mr Cameron will not be able to win his reform battles by stealth and charm alone. He needs steel and stomach for what lies ahead.

The inflation scare

The long blip

Jan 20th 2011 | from PRINT EDITION

Higher prices are squeezing consumers rather than sparking pay rises

THE script for 2011 had been well rehearsed. The Treasury's fierce fiscal retrenchment would undoubtedly hurt the economic recovery. But the Bank of England would add balm by maintaining an extraordinarily loose monetary stance. Just three weeks into the new year, however, surging inflation has disrupted the story. The worry is that this could endanger the recovery by forcing a premature tightening in monetary policy.

Official figures out this week made uncomfortable reading for the central bank, which has the task of meeting the government's 2% inflation target. They showed consumer prices rising by 3.7% in the year to December, up from 3.3% in November. The outcome was a lot worse than the 3.4% rate that City economists had predicted. The upward lurch largely reflected higher fuel and food prices. The price of petrol at the pump reached a record high of pound1.22 ($1.90) a litre, home gas and heating-oil bills increased and food-price inflation went up from 4.9% to 5.7%.

Throughout 2010 inflation ran at or above 3%. That is a pretty dismal record, but it will get even more wretched this year as inflation heads above 4%. For on January 4th, the main rate for VAT, a consumption tax, was raised from 17.5% to 20%. While some retailers might already have jumped the gun, the main effect of the tax rise will be felt in early 2011. When VAT went up a year ago only about half of the increase was passed on to prices. This time virtually all of it is expected to go through to prices.

But a jump in inflation caused by higher commodity prices and a rise in VAT-in an economy with spare capacity-is quite different from one caused by excess demand and a pay-price spiral. It intensifies the squeeze on households from other tax rises and curbs consumer spending. Although the central bank is facing calls to tighten monetary policy soon, that would be warranted only if there were signs of inflation getting embedded into expectations and feeding through to higher wages.

Unsurprisingly, households are now expecting inflation to be higher over the coming year. But other official figures published this week showed no sign of a pay-price spiral. Average earnings are rising by just 2.1%, a very muted rate by historical standards. It is difficult to envisage wages taking off when the public sector is shedding jobs and facing a two-year pay freeze and there are 2.5m people unemployed, close to 8% of the labour force. Indeed the youth-unemployment rate has reached 20.3%, the highest since comparable records began in 1992.

The economy clearly retains quite a bit of spare capacity-the main reason why the Bank of England has insisted that the flare-up in inflation will be temporary. The bank has lost credibility as the inflation overshoot has persisted and its forecasts have proved incorrect. But the best way to regain its credentials is not to make a panicky move now but to hold its ground, tightening policy only when it is clear that the recovery can cope with the fiscal clampdown. That should be apparent by late summer. And that is when the bank is likely to start restoring more normal monetary settings, by raising the base rate from its all-time low of 0.5%.

Index | Britain

Burberry and globalisation

A checkered story

Jan 20th 2011 | from PRINT EDITION

Burberry's revival reflects the potential of globalisation, and its limits



A long way from the football terraces

FOR Britons wondering how their country will earn its keep in a world that is tilting eastward, some sectors offer cause for optimism. Newly prosperous foreigners will probably want at least a few things that Britain supplies better than most: higher education, financial services, popular culture. Another, sometimes underestimated strength is fashion: the country boasts influential street stylists and vibrant chain-stores (such as Top Shop), plus some coveted luxury brands, such as Burberry.

On January 18th the 155-year-old label announced a 27% jump in revenue to pound480m ($770m) for the last quarter of 2010. Burgeoning sales in Asia (amounting to pound150m, up 68% on the same quarter a year earlier) accounted for much of this. Burberry recently bought 50 shops in China that had previously been run by its franchise partners, and would like to open more there. Latin America is another important growth area; new outlets have recently been opened in Brazil and Mexico. Even in Britain, where there are just a handful of stand-alone Burberry shops, the company's best customers are foreign tourists.

On the face of it, none of this is surprising. Many luxury-goods manufacturers are profiting from the rise of the Asian rich. But Burberry's story is more interesting than that of many posh brands. For in its own backyard, the firm has had to fight to preserve its reputation for exclusivity.

The problem dates back to the 1980s, when football fans travelling to European cities for matches took a liking to the snazzy clothes sported by the locals. By hook or by crook, they returned home with these garments: Lacoste polo shirts, Sergio Tacchini sweaters, Fila shoes and so on. Thus the "casual" movement was born: a culture of sartorial one-upmanship on football terraces, in a country where working-class men obsessed over clothes long before the rise of the metrosexual. The more patriotic of these casuals began to adopt home-grown brands, and Burberry, previously the preserve of greying executives on golfing holidays, became a favourite.

By the early 2000s the company's distinctive camel-coloured check had become the uniform of the "chav", the stereotypical white working-class delinquent looking for trouble. Bouncers and taxi drivers learned to turn away young men sporting Burberry baseball caps and jackets. When Daniella Westbrook, a soap actress, was photographed with the Burberry check adorning herself, her daughter and her pushchair, the brand's elite reputation seemed to be lost.

Painstakingly, and without much outward snootiness about its new and unexpected clientele, Burberry fought back. The check pattern began to appear less and less on its garments. The company cracked down on vendors selling counterfeit versions of Burberry clothes at discount rates. More daring designs were adopted to court opinion-formers in the fashion world (Burberry had traditionally specialised in trench coats and other well-made basics). Two American women are credited with bringing about many of these changes: Angela Ahrendts, the company's current CEO, and her predecessor, Rose Marie Bravo.

In Britain the brand has been largely mended. Abroad it was hardly tainted in the first place. Foreigners continued to see Burberry as the august outfit that clothed Ernest Shackleton for his Antarctic expedition nearly a century ago, not the favoured label of a subculture they could barely comprehend. Modern economics and technology allows Chinese, Brazilian and American consumers to buy the wares of a London firm. But it has not made it that much easier to grasp the cultural nuances of another country. Had Burberry's chav association been known abroad, the damage would have been greater, and the brand might have been harder to turn around. Burberry has benefited from globalisation, and from its limitations too.

Cheap booze

Getting (a wee bit) dearer

Jan 20th 2011 | from PRINT EDITION

A minimum price for alcohol is unlikely to affect drinking habits-for now



IT IS always faintly worrying when a trade association calls allegedly crusading legislation a "pragmatic solution". On January 18th the sigh of relief with which the Wine and Spirit Trade Association greeted government plans to impose a minimum price on alcohol in England and Wales was almost audible. Less than a year ago, in their coalition agreement, the Conservatives and Liberal Democrats had pledged to ban the sale of alcohol below cost price. In the event, they have settled for banning sales of drink for less than the tax paid on it (alcohol duty, plus VAT, a consumption tax). Tesco, the country's largest supermarket chain, called the measure "reasonable".

Anti-alcohol campaigners are less enchanted. The proposal would require a minimum price of about 21p ($0.34) per unit of beer (hence 38p for a 440ml can of weak lager), or 28p per unit of spirits (eg, pound8 for a 700ml bottle of whisky). Dr Ian Gilmore, of the Alcohol Health Alliance UK, a pressure group, calls the move "a step in the right direction but...an extremely small step". Don Shenker, of Alcohol Concern, thinks a minimum price of at least 40p per unit might begin to affect behaviour. Scotland's Parliament came close to adopting a 45p minimum last year (the proposal was voted down), and a much-discussed study in 2008 by academics at Sheffield University thought 50p was the lowest that should be contemplated.

But if imposing a minimum price on alcohol is the solution, what, precisely, is the problem? Per capita tippling in Britain is only the 12th-highest in the European Union, according to the World Health Organisation. Although British consumption has more than doubled over the past 50 years (thanks in part to plummeting costs, as determined drinkers tank up at home on cheap supermarket-bought liquor before heading out to club or pub), it is still lower than it was at the beginning of the last century. And the latest official figures suggest that drinking is already tapering off anyway: a bit less was imbibed in 2008 than before and sales of alcopops, the downfall of many a teenage girl, had slipped. More medicine was prescribed in 2009 to wean people off booze.

Against this possibly rosy view, campaigners point out that a lot of people in Britain, some 12%, are teetotal (starting with most Muslims, whose numbers are increasing), which means that those who do drink consume more than overall figures suggest. But the core of the argument is binge drinking: Britons may not down that much overall, but when they do, some run amok, and everything from violence to serious health problems result.

The incidence of chronic liver disease and cirrhosis, falling in Spain, France and Italy, is rising in Britain. Almost 7,000 deaths in England in 2008 were directly attributable to alcohol, according to official figures; government attempts in 2003 to estimate the broader costs of excess drinking-to the NHS, to employers, to society in the form of anti-social behaviour-came up with over pound15 billion, in 2001 prices.

Will this new minimum price change much? Perhaps not: many retailers say they charge more than the minimum now. But there are two reasons to think it might. Young drinkers are likeliest to be restrained by higher prices on cheap booze, and they are also likeliest to throw punches and get pregnant. And once the principle of a minimum price has been established, the government or its successors can raise it.

Index | Britain

Rape and prostitution

In from the cold

Jan 20th 2011 | from PRINT EDITION

Sex workers, the biggest victims of rape, are starting to report it more

AGAINST a background of generally falling crime, recorded rape rose by almost a quarter in London last year, the Metropolitan Police said on January 18th. English and Welsh figures for 2010-11, due for release in July, are likely to show a similar pattern: in the year to March 2010 rape complaints were running 15% higher than in the same period a year earlier, with rape of girls under 13 up by more.

Though not a week goes by without stories of "grooming" gangs and rogue taxi drivers, these statistics are better news than they seem. Most analysts think they show that rape is more reported and recorded than before, not that it is markedly more prevalent. Changes in the sort of specialist support victims receive, and in police attitudes, mean that more of those who are raped (perhaps 60,000 a year, on Home Office estimates) are coming forward. In 2007-08 the British Crime Survey put the proportion of women reporting a serious sexual assault at a measly 11%.

In the past sex workers have been especially slow to call on the law. Many are in trouble themselves: soliciting is illegal, though selling sex isn't, and some might be wanted for shoplifting to feed a drug habit, or for immigration offences. Probably most fear people will think that, because they sell sex, they have rape coming to them.

Yet women working in prostitution are at particular risk of violence, especially the 20,000 (overwhelmingly white British and dependent on hard drugs) who walk the streets. Shelly Stoops, a project worker in Liverpool, reckons about three-quarters of street prostitutes there have been assaulted and almost half have been raped at least once. Until recently, very few have seen fit to tell the police.

A new approach is beginning to help. Around five years ago, with five unsolved murders of sex workers on their books, the Merseyside police decided to focus more on preventing harm and less on enforcing anti-soliciting laws. To solve such crimes and forestall more, evidence from prostitutes was vital-and, as Detective Inspector Tim Keelan points out, "people who attack sex workers don't only attack sex workers." Women had to believe that assaults on them would be taken seriously, and their own minor misdeeds overlooked.

So the police intensified their partnerships with outfits working with prostitutes, particularly the Armistead Street Project, part of Liverpool's community-health service. In 2006 Ms Stoops became Britain's first specialist Independent Sexual Violence Adviser (ISVA) for sex workers. By night she and her team cruise the streets like modern Gladstones, offering working girls coffee and condoms, fresh needles and advice about what to do in case of assault. By day they staff drop-in clinics, accompany women through the maze of the criminal-justice system and update their "Ugly Mugs" file of known local thugs.

As a result of such measures, and of closer co-operation between police and prosecutors, the number of sex workers who report attacks to the police has shot up, and so have convictions. Between 2007 and 2010, 80% of those charged with offences against a prostitute were convicted, says Ms Stoops, and 67% of those charged with rape (nationally, for all victims the rate is some 58%). In the five years to 2007, one person was convicted for assaulting a prostitute in Liverpool.

The "Merseyside model" is spreading. Last year the Home Office funded ISVAs in sex-worker projects in other cities. One of these, Open Doors in London, helped to secure a conviction for rape this month. Modestly more funding is on the cards.

And next week Ms Stoops and others will present research to the Home Office buttressing a bid for a sophisticated, nationwide "Ugly Mugs" scheme, to help sex workers avoid harm and police to investigate reports more quickly. The Conservatives, with their traditional emphasis on the sanctity of family life, might not be obvious enthusiasts for the project. But "it's not about ideology," says Ms Stoops. "It's about protecting people."

Index | Britain

Education maintenance allowances

A hand-up, not a handset

Jan 20th 2011 | from PRINT EDITION

Better prospects might keep youngsters in school more effectively than bribes



At least he can spell

SHORT of simply forcing them to remain in education, how should young people be encouraged to better themselves? One idea, implemented by the previous Labour government in 2004, was to introduce an "education maintenance allowance", which paid up to pound30 a week for college attendance to 16-18-year-olds from families with an annual income of pound30,810 or less. The money was supposed to persuade parents who would otherwise push their offspring into low-paid manual work to direct them into training instead.

Yet a study commissioned by the previous government and published just before last year's election found that only 12% of the teenagers receiving the allowance said they would not be able to attend college without it. That was seized on by the incoming education secretary, Michael Gove, who is abolishing the allowance in England (but not in Scotland, Wales or Northern Ireland). On January 19th, in the latest bout of youthful anti-austerity demonstrations, students across England protested against the decision as MPs debated it.

Some 650,000 teenagers-almost half of all youngsters in post-compulsory education-claim the allowance. The money was supposed to be spent on bus fares, books and the like, but some recipients have frittered it away on fripperies such as make-up and mobile phones. Reports of ne'er-do-wells showing up to claim the allowance but skipping classes were given credence by the fact that the money was handed out whether or not the recipient also had a part-time job.

The Institute for Fiscal Studies, a think-tank, nevertheless reckons that channelling pound560m a year into poor families in this way was worthwhile. It calculated that the money wasted on the 88% of recipients who would have attended college anyway was outweighed by the savings made (in welfare benefits) on the 12% who wouldn't have.

Mr Gove says he will better focus the limited funds available on the particularly needy. But he thinks the best way to boost young people's prospects is to increase the proportion of pupils who leave school with five good GCSE exam passes in traditional subjects. Just 16% of children achieved that last year. A well-educated population with an improved outlook would not need bribes to better itself, he reckons.

Index | Britain

Transparency and the state

Fiat a little more lux

Jan 20th 2011 | from PRINT EDITION

The coalition hopes to build on one of Tony Blair's biggest regrets

"YOU idiot. You naive, foolish, irresponsible nincompoop...I quake at the imbecility of it." So Tony Blair berates himself in his memoirs for passing the Freedom of Information Act (FOIA), which came into force in 2005. The realities of power transformed him from an advocate of official openness into a despairing critic.

Mr Blair's jaded attitude seems not yet to have infected the coalition government, which is planning to let a little more light into the tenebrous corridors of Whitehall. In opposition, both David Cameron and Nick Clegg, the deputy prime minister, promised to promote transparency. It is a cause that Mr Clegg's Liberal Democrats have long championed, arguing that it will improve the workings of government, while the Tories see informed citizens and an open state as essential conditions of their plans to devolve power.

To those ends, the government intends to broaden the scope of the FOIA, extending it to currently uncovered parts of the state, among them the Association of Chief Police Officers, an outfit that sets much policing policy, as well as the regulators that oversee many privatised industries. The government also plans to reduce the length of time that official records remain sealed from 30 years to 20 (the rule looks rather quaint now that former ministers publish tell-all memoirs within months of leaving office).

Other changes are already revealing more details of how government works. The Downing Street website features a new "transparency" section that discloses, among other things, which lobbyists and potentates are meeting which ministers and when. All central-government spending of more than pound25,000 must be published, as well as local government spending of over pound500. The government is keen, at least in theory, to make available much of the data that it holds, for the perusal and analysis of "armchair auditors" and enthusiastic nerds (see article).

Britain's small but vocal freedom-of-information lobby has given the plans a cautious welcome. Maurice Frankel, who runs the Campaign for Freedom of Information, is heartened that the government has pressed ahead despite having plenty of other things on its plate.

Nevertheless, much will remain whelmed in mystery. Messrs Cameron and Clegg both promised before the general election that the new regime would cover Network Rail, an oddly constituted body laden with publicly backed debt that runs Britain's railway tracks. That idea seems to have been ditched. Northern Rock, a bank nationalised in 2008, will escape scrutiny; the rules concerning the royal family are to be tightened. Private firms that administer parts of the NHS, criminal justice, schools and other public services will also be exempt (Scotland, which has separate laws, is considering making big contractors subject to FOI requests).

And changing the rules might not, by itself, fix a cultural resistance to scrutiny within some bits of government. Heather Brooke, a journalist who did much of the spadework that led to the revelations over dodgy expense claims by MPs, thinks that parts of the British state are run "almost feudally," and remain resistant to explaining their workings to mere voters. She argues that better enforcement of the existing system would do more to inform the public of what is done in its name than fiddling with it. That might be a vain hope: the Information Commissioner's Office, which enforces the Freedom of Information Act, has a hefty backlog of cases-and, under the government's austerity plans, is facing cuts.

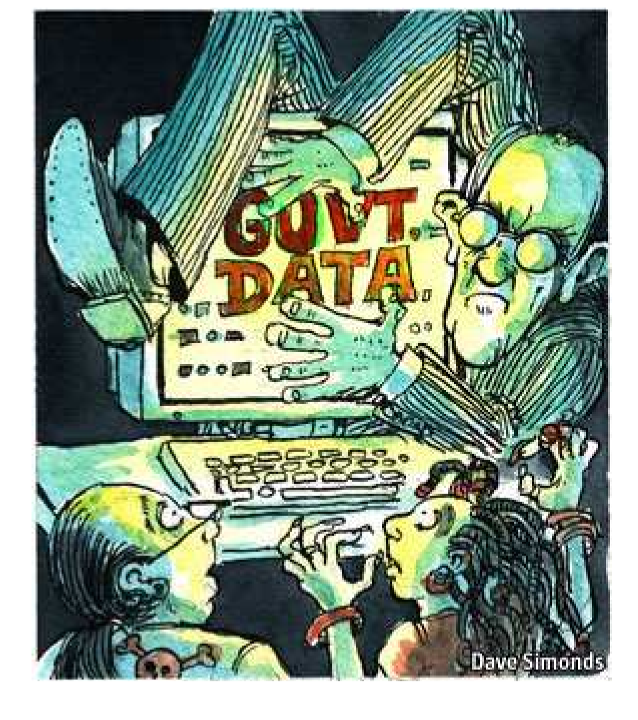
Index | Britain

Recycling government data

Bit by bit

Jan 20th 2011 | from PRINT EDITION

The government wants to set its data free-in theory



ON A website called traintimes.org.uk, users can inspect a map of Britain crawling with little red dots. Each dot represents a train on the national network; visitors can filter the map to see all the trains bound for a particular station. Another site, openlylocal.com, lists spending information, council meetings and socioeconomic statistics for local authorities up and down the country. TheyWorkForYou.com has spent six years tracking the voting records of every MP in the House of Commons, information that was previously only available by trawling laboriously through back issues of Hansard.

These sites collate publicly available information and present it in a user-friendly way. All are free, the brainchildren of civic-minded, computer-savvy people. If there is an electronic version of David Cameron's "Big Society", such outfits are surely it.

Inspired by their example, the coalition government, like its Labour predecessor, wants to make much of the data held in musty repositories throughout government freely accessible to the public (which has, after all, paid for its collection). On January 12th the government announced the formation of the Public Data Corporation (PDC), intended to group all the relevant information in one place.

Yet the PDC's reception among Britain's data mavens was distinctly chilly. They point to worrying language about "charging" for information held by the PDC, which seems distinctly at odds with the government's policy of ready access. Chris Taggart, who developed openlylocal.com and sits on a government committee on open data, says that he and his fellow datanauts were taken aback by the announcement.

Mr Taggart suspects a power struggle, either between departments (he says the new PDC is the brainchild of the business department, rather than the Cabinet Office, which is nominally in charge of the data agenda), or between ministers and civil servants. Anyway, freeing up public data can be controversial. Many institutions that hold important information-such as Ordnance Survey, which maintains maps of the country, or the Met Office, which keeps weather records-are run as "trading funds", meaning that they must earn at least half of their income from selling the information they collect.

Many data enthusiasts would like to see the trading funds brought back under central control and their information made available to all. But with ministers trying desperately to cut spending, that seems unlikely to happen. Advocates of openness must await the outcome of the bureaucratic infighting-and hope that the cause of transparency wins.

Index | Britain

Bagehot

The Gruffalo years

Jan 20th 2011 | from PRINT EDITION

A striking number of Britain's senior politicians have young children. That is a good thing



THEY begin-painfully-with Tinky Winky and Igglepiggle. They end somewhere near Narnia, or Hogwarts. For millions of middle-class Britons they are perhaps best described as the Gruffalo years: an innocent interlude stretching from birth to a child's ninth birthday or so. Barring tragedies, children in these years inhabit a sheltered, more benign world-and fortunate parents enjoy visiting rights. With luck, outside horrors can be kept at bay. Parents are not yet embarrassing, and a bedtime book is still a treat: the Gruffalo, a dimwitted monster, is a particular British hit. It is an age before tests turn brutal, when a child's life still shines with potential. Time enough for failure later.

A striking number of senior politicians live, at least part-time, in the world of the really young. David Cameron, the prime minister, his Liberal Democrat deputy Nick Clegg and the Labour leader, Ed Miliband, all have infants under two years old, and none has a child older than nine. Members of the coalition inner circle such as George Osborne, the chancellor of the exchequer; Steve Hilton, the Downing Street director of strategy; Michael Gove, the education secretary; and Danny Alexander, the Lib Dem chief secretary to the Treasury have families just as young.

The nappy-changing diligence of Mr Cameron, Mr Clegg and Mr Miliband should not be exaggerated. All three work ferocious hours and can afford child care. Mr Cameron has family money; Mr Clegg and Mr Miliband have high-flying lawyers as partners. But all three try to carve out time for their children. Mr Cameron's family lives above the shop in Downing Street. Mr Clegg works late but walks his two older sons to school when he can. Mr Miliband holds many meetings at his north London home. This is both engaging (as when the Labour leader talks strategy with a baby on his knee), and time-consuming (as when his toddler swiped guests' mobile phones at a recent gathering).

Part of the explanation is the youth of Britain's rulers: Mr Cameron was the youngest prime minister to take office in nearly two centuries; the main party leaders are in their early 40s. The professional middle classes as a whole are having children later. The child-bearing trend began in 2000, when Tony Blair sired the first baby born to a serving prime minister in more than 150 years. But he also had teenage children, so had been dunked in the stormier waters of adolescence. A turning point came with Gordon Brown's coronation as Labour leader in 2007. Though in his 50s, Mr Brown had two very young sons (his first child died shortly after her birth in 2001). Suddenly all three party leaders were new parents. What is more, the younger men in Mr Brown's cabinet were keen to be active fathers, adds a figure close to Mr Brown and Mr Miliband. It was "a massive cultural change compared to ten years before".

A centrist Conservative MP makes a matching observation about the youthful circle around Mr Cameron. The Tory party of ten years ago was slow to grasp the importance of social policies. For today's leadership, children are the "ultimate nudge", he says, a reference to the Cameron camp's zeal for "nudging" people into changing behaviour. At its simplest, parenthood exposes even the affluent middle classes to public services, from hospitals to day-care centres or libraries. Despite (mostly) shielding their children from press attention, all three current party leaders claim inside knowledge of the National Health Service and the strains of balancing work and family life.

Launching a vast reform of the NHS on January 17th, Mr Cameron-as often before-cited his biography as proof of his good faith, praising the doctors who cared for his severely disabled eldest son (who died aged six in 2009), the maternity nurses who recently helped deliver his baby daughter and the teachers "currently inspiring" his two other children at primary school. On the same day, Mr Clegg vowed to help fathers be more "hands-on" with their children, whether by taking more parental leave or seeking flexible working hours. On January 15th Mr Miliband apologised for the previous Labour government's embrace of labour laws that had squeezed "time with our families".

With close advisers, the Labour leader has pondered the politics of parenthood: does it make people more conservative, by which he means competitive and sharp-elbowed? Or perhaps (Mr Miliband hopes) parenthood induces empathy and trust, as even flinty individualists find themselves grateful to nannies, doctors or the BBC, with its wholesome children's programmes.

Smugger but wiser

Daily exposure to innocence matters. Parenthood can lead to smugness, but also humility. All parents soon realise how much of child-rearing is improvisation, tempered by exhaustion. Political parents learn that ideology is not everything. The coalition leaders use state primary schools. But in interviews, Mr Clegg (who like Mr Cameron was privately educated) has reserved the right to send his boys to a fee-paying secondary school, saying he is a father before he is a politician. Though the three are social liberals, parenthood has exposed flashes of conservative anxiety. Mr Cameron frets about rude pop lyrics and "sexy" clothes aimed at children. Mr Miliband says this is the first time in 100 years that parents fear the next generation will be worse off.

The importance of the Gruffalo years unites all three parties. The Tory-Lib Dem coalition has published reports from two Labour MPs, Frank Field and-most recently-Graham Allen, urging "early intervention" to help deprived kids from birth. Some Tory ministers grumble that 16-to-25-year-olds have been a bit forgotten by the coalition. That may be right, yet on balance young parenthood is healthy for Britain's rulers. The world looks at once kindlier and more fragile with small children in it, and essentially optimistic. In these austere times, that is a source of strength.

Economist.com/blogs/bagehot

Index | International

Inequality

Unbottled Gini

Jan 20th 2011 | from PRINT EDITION

Inequality is rising. Does it matter-and if so why?



FOR the head of the IMF to quote Adam Smith may seem unremarkable. But here is Dominique Strauss-Kahn citing the great man in November 2010: "The disposition to admire, and almost to worship, the rich and the powerful and...neglect persons of poor and mean condition...is the great and most universal cause of the corruption of our moral sentiments."

Mr Strauss-Kahn then bemoaned "a large and growing chasm between rich and poor-especially within countries". He argued that inequitable distribution of wealth could "wear down the social fabric". He added: "More unequal countries have worse social indicators, a poorer human-development record, and higher degrees of economic insecurity and anxiety."

That marks a huge shift. Just before the financial crisis America's Congress was gaily cutting taxes for the highest earners, and Tony Blair, Britain's prime minister, said he did not care how much soccer players earned so long as he could reduce child poverty. So why has fear of inequality stormed back into fashion? Does it matter in some new way? Does it have previously unknown effects?

The most obvious reason for the renewed attention is inequality's apparent increase. A common yardstick is the Gini coefficient, which runs from 0 (everyone has the same income) to 1 (one person has all the income). Most countries range between 0.25 and 0.6.

The Gini coefficient has gone up a lot in some rich countries since the 1980s. For American households it climbed from 0.34 in the mid-1980s to 0.38 in the 2000s. In China it went up even more, from under 0.3 to over 0.4. But this was not universal. For decades, Latin America had the world's worst income inequality. But Brazil's Gini coefficient has fallen more than five points since 2000, to 0.55. And as poor countries are on average growing faster than rich ones, inequality in the world as a whole is falling.

Getting richer quicker

Greater inequality can happen either because the wealthier are getting wealthier, or the poor are falling behind, or both. In America it has had more to do with the rich. The income of the wealthiest 20% of Americans rose 14% during the 1970s, when the income of the poorest fifth rose 9%. In the 1990s the income of the richest fifth rose 27% while that of the poorest fifth went up only 10%. That is a widening income spread, but not a drastic one. Robert Gordon, an economist at Northwestern University in Illinois, reckons that for the bottom 99% of the population, inequality has not risen since 1993.

The problems at the bottom are reasonably well understood: technology enables the automation of blue-collar trades; globalisation lets unskilled jobs move to poorer, cheaper countries; shrinking trade-union membership erodes workers' bargaining power. But inequality is rising more sharply at the top, among what George Bush junior called the "haves and have-mores". Here the causes are more mysterious.

The economists Emmanuel Saez and Thomas Piketty studied the incomes of the top 0.1% of earners in America, Britain and France in 1913-2008. America's super-rich, they found, were earning about 8% of the country's total income at the end of the period-the same share as during the Gilded Era of the 1920s and up from around 2% in the 1960s. A study by the Economic Policy Institute, a think-tank in Washington, DC, looked at the ratio of the average incomes of the rich and

the "bottom" 90% of the population between 1980 and 2006. It found that the top 1% earned ten times more than the rest at the start of the period and 20 times as much at the end-ie, its "premium" doubled. But for the top 0.1% the gain rose from 20 times the earnings of the lower 90% to almost 80-fold.

You can understand why people might regard this as unfair: the top 0.1% do not seem to be working 80 times as hard as everyone else, nor are they contributing 80 times more to welfare. But that is a matter of public opinion, and mostly of politics. The question of the economic impact of extreme inequality is separate. Recent evidence suggests it may not be as damaging as many imagine. Our special report casts doubt on the widespread view that inequality causes (or is associated with) a host of social problems. Economics focus finds little evidence that it stoked the financial crisis.

But recent research does suggest two other reasons why the rise in inequality is a problem. One is that rich economies seem to provide disproportionate and growing returns to the already wealthy. The other is that inequality may literally be making people miserable by increasing stress and the hormones it releases.

In a recent series of lectures at the London School of Economics, Adair Turner, the chairman of Britain's Financial Services Authority, cited several factors that appear to be pushing up the incomes of the rich. First, financial, legal and health services have increased their shares of GDP in most rich economies-especially Anglo-Saxon ones-and these professions contain some of the richest people in the country. Financial services' share of GDP in America doubled to 8% between 1980 and 2000; over the same period their profits rose from about 10% to 35% of total corporate profits, before collapsing in 2007-09. Bankers are being paid more, too. In America the compensation of workers in financial services was similar to average compensation until 1980. Now it is twice that average. Rich bankers really are all around you.

Turner turns the screw

Next, argues Lord Turner, as people get wealthier they tend to devote more discretionary income to what are called "positional goods"-items such as limited-edition, celebrity-endorsed sneakers whose main value lies in their desirability in the eyes of others. The willingness of people to buy such stuff, combined with the vast new markets of millions of emerging middle-class consumers in China, India and elsewhere, has boosted the stars' brands beyond anything that was possible in the past. Bobby Jones, the best golfer of the 1920s, was an amateur. Tiger Woods earned $90m in 2009, before sex scandals wrecked his image. Writing children's novels used to keep authors in chintz and twinsets. J.K. Rowling, author of the Harry Potter books, is a billionaire.

Admittedly, truly global celebrities are few in number. But they have a penumbra of agents, lawyers and image-makers. As Lionel Robbins, a British economist, once said, "a substantial proportion of the high incomes of the rich are due to the existence of other rich people."

The growth of celebrity rents explains more than just why there may be more rich people around. The point about positional goods-and of fashion and brands in general-is their relative attractiveness. Owning the latest gadget or garment is particularly attractive when others don't have it, rather as buildings are valuable because of their location: ie, how desirable they seem to others. With such goods, a rising tide does not lift all boats. You yearn to be not merely richer, but richer than your neighbours. So the more brands, fashion and houses become important, the more relative income and inequality matter.



This would seem to qualify one of the commonest justifications for being relaxed about inequality: that it is not a big concern if the rich are getting richer so long as the poor are doing well too. That view was shared by Margaret Thatcher and Ronald Reagan and more recently by Mr Blair and Ben Bernanke, the Fed chairman. But if positional goods are taking a larger share of people's salaries, then relative income does matter and so do income disparities between rich and poor. Positional goods do not affect material welfare, as do poor schools or substandard housing. But they do affect people's quality of life and well-being. That leads to a second reason for worrying about inequality: its physiological and physical consequences.

In "The Spirit Level", a bestselling book of 2009, Richard Wilkinson and Kate Pickett argue that inequality "gets under the skin" and makes everyone worse off, not just the poor. They mean "gets under the skin" literally. The argument is that inequality causes chronic stress, and makes people secrete too much of a hormone called cortisol. This normally has benign metabolic and other functions. Produced in large quantities it can harm among other things the brain and the immune system. So cortisol may be a direct link between inequality and bad health.

Another is that inequality impairs the production of a second hormone, oxytocin. Sometimes referred to as the "cuddle hormone", this is secreted in childbirth and during breastfeeding, and seems to encourage pair-bonding and trust in others. The claim is that people living in unequal societies secrete less oxytocin, hence they have lower levels of trust. These accounts might be dubbed the medical, as opposed to material, explanations for inequality's bad effects.

The hypothesis is plausible. Humans are social animals and have been refined by evolution to be extremely sensitive to social interactions. Though intuitively attractive, the link is not yet well established. Most studies of hormonal stress markers have focused on particular groups subject to huge, chronic woes, such as carers of patients with Alzheimer's disease. Little research so far has dealt with the general population. A recent review of the scientific literature found little consistent evidence of a link between bio-markers of stress and social or economic status.

Nor is it certain that income inequality is the right problem to focus on. What seems to affect levels of stress hormones is not income, but competition for status, a broader, fuzzier notion. Evolution has primed humans to seek high status. Losers in competitions for esteem may well suffer. Societies with fierce status competition may well be unhealthier and more violent. But it is the disparities of status, not of income, that matter.

Often the two go together: Nordic countries have low income inequality and not too much status competition. But one can also imagine societies with narrow income disparities that are riddled with status conflict. The old Soviet Union is a vivid example. The inverse is conceivable too: countries with large income disparities but less status conflict, perhaps because competition is smoothed by social mobility. Arguably America fitted that description until recently. Overall though, it is true that in most places growing income disparities are a reasonable proxy for growing status competition.

Economists have long argued that inequality is a much less important problem than poverty. The recent research linking inequality to widespread social ills has not decisively overturned that view: the evidence is still mixed, at best.

The claim that inequality now matters more because of brands and status competition may turn out to be more robust. Such concerns could seem peripheral compared with global woes such as poverty. But inequality is local. As Adam Smith also once wrote, "if he was to lose his little finger tomorrow, he would not sleep tonight; but provided he never saw them, he would snore with the most profound security over the ruin of a hundred million of his brethren."

Correction: The Indian army

Jan 20th 2011 | from PRINT EDITION

The table in "War's overlooked victims" (January 13th) mistakenly blamed the Indian army, rather than Pakistani forces, for 200,000 rapes in 1971. We apologise.

A special report on global leaders

The few

Jan 20th 2011 | from PRINT EDITION

In the information age, brainy people are rewarded with wealth and influence, says Robert Guest. What does this mean for everyone else?



TOMMY GALLAGHER was working across the street when the planes hit the Twin Towers. "As we evacuated, we could see people jumping out of windows," he recalls. Then the first tower collapsed. Everyone in the street started running. A huge cloud of dust enveloped them. Mr Gallagher could not see or breathe. He thought he was going to die.

Soon after he escaped, Mr Gallagher was told to put his bank's business back together at an office in uptown Manhattan. Plugging the computers in again was easy enough, but the people in the office could not simply be re-booted. After a month Mr Gallagher snapped. "A guy gave me shit. I threatened to beat him up. They fired me," he says.

He was 57 at the time. "On Wall Street, you're an old man at 50," he shrugs. He could not find another job. Financially that did not matter much: he was a wealthy man. But emotionally he was "a basket case". He was embarrassed about having been fired, ashamed of his behaviour and "absolutely alone". He started worrying that the doormen at his fancy apartment must be thinking: "That guy's a loser."

Then he joined a self-help group for rich people called Tiger 21. Only those with more than $10m of investable assets are eligible for membership, so no one assumes that, just because you have truckloads of cash, your problems are trivial. Whether you are worried that your kids might turn out like Paris Hilton, or fed up with your brother-in-law wanting to borrow money for the umpteenth time, someone in the room has faced a similar problem before.

Mr Gallagher credits Tiger 21 with helping him to find a new purpose in life: philanthropy. Many other members are veteran givers, and advise him on how best to support his pet cause, which is caring for military veterans with post-traumatic stress disorder. His son served as a counter-intelligence officer in Afghanistan and had to calculate the power of roadside bombs by measuring how far they threw pieces of their victims' bodies, so Mr Gallagher has a personal interest in this. He is now on the board of Phoenix House, a mental-health charity, and is involved in a programme to stop traumatised veterans from drifting into divorce, homelessness and suicide.

The new elite

This special report is about global leaders, but mostly not the sort you have heard of, such as presidents and pop stars. Instead, it looks at the people who shape the world without anyone noticing: those with enough brains, money or influence to affect the lives of large numbers of others. These three things often go hand in hand, but not always.

Some people are influential because they have compelling ideas or are skilled at popularising other people's. The brainy toilers at think-tanks in Washington, DC, do not earn nearly enough to be admitted to Tiger 21, but they wield immense influence over public policy. The propagandists of al-Qaeda live in caves, but affect the lives of people everywhere.

Societies have always had elites. For most of history and in most countries, power was seized by force of arms and passed down from father to son. Fear and heredity still play a role. China's ruling party remains in charge because it jails and occasionally kills those who threaten it. America elected two presidents named George Bush and came close to electing two Clintons.

The big change over the past century is that elites are increasingly meritocratic and global. The richest people in advanced countries are not aristocrats but entrepreneurs such as Bill Gates (pictured above with his wife and partner in philanthropy, Melinda). The most influential are those whose inventions change lives in many countries (think of Facebook) or whose ideas are persuasive (think of Amnesty International).

This special report will examine how influence is wielded. It will look at the minds that shape politics, business and technology, and it will describe the gatherings where influential people swap ideas, from the World Economic Forum in Davos to Nathan Myhrvold's "invention sessions" in Seattle.

The global elite are a cosmopolitan bunch, yet they are far from rootless. Indian tycoons forge deals with ethnic Indians throughout the world. Chinese scientists in Beijing collaborate with Chinese scientists in Cambridge. The report will show how money, ideas and influence flow through the world's diaspora networks.

It will also look at inequality, which has risen relentlessly in most rich countries even as they have become more meritocratic. Clever, well-educated people are increasingly marrying each other and raising clever, well-educated children. The children of ordinary households find it hard to compete with them. A new aristocracy of merit is emerging. That has social consequences for everybody.

Serious thinkers sometimes exaggerate the clout of the few. David Rothkopf's book "Superclass: The Global Power Elite and the World They Are Making" is thoughtful and well researched, but his breathless description of how a mere 6,000 politicians, chief executives and other bigwigs run the world misses an important point. In democracies at least, the few are often at the mercy of the many. Voters can get rid of politicians they dislike. Consumers will stop buying a company's products the moment something better or cheaper comes along. In a democracy with a competitive economy, power is hard to maintain without pleasing others.

In China the rules are different. Economic growth has lifted hundreds of millions of Chinese people out of poverty and made China's coastal cities rich. But the Chinese elite depends too much on the coercive power of the Communist Party for its wealth and influence. The system of *hukou* (residence permits) creates two classes of citizen, urban and rural. As in South Africa under apartheid, those on top dictate where those at the bottom may live and work, suppressing their wages and providing themselves with cheap servants. This cannot last.

As Mr Gallagher's story shows, the rich are as vulnerable as the rest of us, yet they lead separate lives. In "Richistan", a book written before the financial crisis, Robert Frank observed that wealthy people have "built a self-contained world unto themselves, complete with their own health-care system (concierge doctors), travel network (NetJets, destination clubs), separate economy...and language ('Who's your household manager?')".

Rich folk affect the rest of us in two big ways. First, the way they spend their money has all kinds of ripple effects. Their hunches move markets. Their consumption supports a whole sub-economy of hoteliers, watchmakers and financial advisers. And their philanthropy funds schools, pressure groups and research into tropical diseases.

The second, and more important, way is that to become rich in the first place, they typically have to do something extraordinary. Some inherit their money, of course, but most build a better mousetrap, finance someone else's good idea or at least run a chain of hairdressers in a way that keeps customers coming back. And because they are mostly self-made, today's rich are restless, dynamic and much keener on change than the aristocrats of old.

A special report on global leaders

More millionaires than Australians

Jan 20th 2011 | from PRINT EDITION

Taking stock of the world's plutocrats

MOST people would describe a dollar millionaire as rich, yet many millionaires would disagree. They do not compare themselves with teachers or shop assistants but with the other parents at their children's private schools. To count the number of rich people in the world, however, an arbitrary cut-off point is needed, and $1m is as good as any. Capgemini, a consultancy, defines anyone with investable assets of $1m or more (excluding their home) as a "high-net-worth individual", consultant-speak for rich. By this conservative measure the planet has about 10m millionaires, according to Capgemini and Merrill Lynch, a bank.

Credit Suisse, another bank, uses a less stringent (and more obvious) definition: a millionaire is anyone whose net assets exceed $1m. That includes everything: a home, an art collection, even the value of an as-yet-inaccessible pension scheme. The Credit Suisse "Global Wealth Report" estimates that there were 24.2m such people in mid-2010, about 0.5% of the world's adult population. By this measure, there are more millionaires than there are Australians. They control $69.2 trillion in assets, more than a third of the global total. Some 41% of them live in the United States, 10% in Japan and 3% in China.

How did these people grow rich? Mostly through their own efforts. Only 16% of high-net-worth individuals inherited their stash, according to Capgemini. The most common way to get rich is to start a business: nearly half (47%) of the world's wealthy people are entrepreneurs.

You do not have to be a genius to build a million-dollar business, but it helps if you are intelligent and extremely hard-working. In their book "The Millionaire Next Door", Thomas Stanley and William Danko observed that a typical American millionaire is surprisingly ordinary. He has spent his life patiently saving and ploughing his money into a business he founded. He does not live in the fanciest part of town-why waste money that you can invest? And his tastes are so plain that you can barely tell him apart from his neighbours. He buys $40 shoes, and his car of choice is a Ford.

Another 23% of the world's millionaires got rich through paid work, estimates Capgemini. A few vault easily over the million-dollar bar. Gregory Maffei, the boss of Liberty Media, an American cable-television firm, earned $87,095,882 in 2010. The median pay for chief executives at the 456 largest publicly quoted firms in America was $7.23m, according to the Hay Group, a consultancy. But the vast majority are skilled professionals or managers who have been careful with their money. An orthodontist in America makes about $200,000 a year. He may leave medical school heavily in debt, but after a lifetime of earning, saving and investing, he can probably amass $1m.

Some people hoped that the financial crisis would reduce the clout of the wealthy. In a crude sense it did: many saw a big part of their wealth vaporise. Capgemini says the number of high-net-worth individuals in the world (by their definition) fell by 15% in 2008, to 8.6m. Their total wealth tumbled by nearly 20%, to a still impressive $32.8 trillion, or $3.8m each. The super-rich fared even worse: the number of people with assets of $30m or more fell by a quarter in 2008, and their assets shrank by 24%.

Last year, however, the rich bounced back. By Capgemini's measure their collective wealth rose by 19% in 2009, to $39 trillion. For the first time the number of rich people in Asia was much the same as in Europe: about 3m in each continent. The combined assets of Asia's plutocrats, at $9.7 trillion, actually surpassed the European total. North America's fat cats remained a whisker richer, with $10.7 trillion between the 3.1m of them.

More money, more say

The global wealth pyramid has a very wide base and a sharp point. The richest 1% of adults control 43% of the world's assets; the wealthiest 10% have 83%. The bottom 50% have only 2%. This suggests a huge disparity of influence. The wealthiest tenth control the vast bulk of the world's capital, giving them a lot of say in funding businesses, charities and politicians. The bottom 50% control hardly any capital at all.

That said, this huge group includes people in quite different circumstances. Many young people in rich countries have no assets and a wallet full of maxed-out credit cards. Technically, their debts make them poorer than African peasants who have nothing. But they enjoy a much higher standard of living and far better prospects. In Denmark and Sweden a startling 30% of the population say their debts exceed their assets, but few go hungry. Many have simply taken out large student loans which an indulgent government allows them to repay very gradually.



At the apex of the pyramid there are 81,000 people with assets of more than $50m. Of these, some 30,000 have more than $100m and 2,800 have more than $500m. Nestled into the sharp tip at the top, Credit Suisse reckons there are about 1,000 dollar billionaires (see chart 1).

For a while after the crash, many rich people piled into safe havens. The proportion of their assets securely parked in fixed-income investments rose from 21% in 2006 to 31% in 2010, says Capgemini. They also tended to pull back from unfamiliar environments. Europeans put more of their money into Europe, Americans put more into America and so on. A striking 71% say they still do not trust the regulators who are supposed to prevent crises.

After the crash many of the rich cut back on unnecessary luxuries, particularly the showy sort. Global yacht sales plunged by 45% in 2009, according to Capgemini, and four out of five yachtmakers had to cut back or shut down. But the market for luxury goods is recovering (see article). And looking at the past decade as a whole, fortune has clearly smiled on fortune-builders. Total global wealth (not just that of the rich) rose by 72% between 2000 and 2010, to $200 trillion, says

Credit Suisse. Nearly half of this was due to the dollar's fall against other currencies, but the rest came from economic growth and a rising population. As the number of adults in the world rose from 3.6 billion to 4.4 billion, the average wealth per person rose from $30,700 to $43,800.

Tracking the rise in rich people's assets is not easy. Unlike income, wealth does not have to be declared to the tax authorities. But there is plenty of evidence that, as Credit Suisse puts it, "the past decade has been especially conducive to the establishment and preservation of large fortunes." To get onto *Forbes* magazine's list of the 400 richest Americans in 1995, you needed $418m. Now it takes $1 billion.

Index | A special report on global leaders

A special report on global leaders

Unloading the loaded

Jan 20th 2011 | from PRINT EDITION

Catering to the whims of the rich is big business



Only the little people wear seatbelts

THE seven-star Burj-al-Arab hotel in Dubai is not for those who like their elegance understated. The presidential suite is an explosion of gold, purple, marble and opulence. Some guests prefer it to the even more expensive royal suite (which is $18,000 a night), says a helpful member of staff, because the decor in the royal suite is even livelier.

When you are seriously rich it is hard to spend all your money, but some creative people will help you try. Quintessentially, a firm founded by Ben Elliot, a nephew of the Duchess of Cornwall, specialises in giving the rich whatever they want, wherever they are. Some requests-tea with Britain's queen, for example-can be a bit difficult, says Mr Elliot. But if a client needs a life-size edible cake costume for a birthday bash, or wants to fly along the Great Wall of China, his global network of fixers will fix it.

The financial crisis hurt sales of luxury goods, which fell by 8% in 2009. But Bain, a consultancy, estimates that in 2010 they grew by 10% worldwide, and by an astounding 30% in China, where the boom barely faltered. In the West the rich have cut back on ostentatious baubles and instead gone for experiences, such as yoga retreats in India or personal coaches to teach them about Buddhism, says Milton Pedraza of the Luxury Institute, a consultancy. China's new millionaires have no such qualms. One retailer there started selling Smart cars covered in Swarovski crystals last year.

What the rich lack is time, says a former personal assistant to celebrities. They may decide to go for a weekend in Thailand on the spur of the moment, and the personal assistant has to make it happen. Another popular time-saver is a medical concierge service. PinnacleCare, for example, will send a doctor "to your home, your office [or] your ski chalet", says Bruce Spector, the founder.

Rich people also want help with handling their money. Creating a fortune is often fun, but conserving it can be tedious, says Charles Lowenhaupt, an adviser to the wealthy. A family may have 100 members scattered over multiple jurisdictions and 150 trusts, making tax planning a trifle complex.

Yet the basic problems are the same everywhere. Mr Lowenhaupt recalls an acquaintance from China teaching him a Chinese saying, "rice paddy to rice paddy in three generations". The acquaintance was surprised to learn that other cultures have similar proverbs.

Index | A special report on global leaders

A special report on global leaders

The rise and rise of the cognitive elite

Jan 20th 2011 | from PRINT EDITION

Brains bring ever larger rewards

WHEN the financial crisis struck, says a prominent banker, the women he knows stopped wearing jewellery. "It wasn't just that they were self-conscious about the ostentation. It was because it didn't look good to them any more." He goes on: "There were blogs that had my name, my family's names, my address. There were death threats. You'd think this could be some pimply kid in a basement, but John Lennon met some pimply kid from a basement. And the kid shot him."

The crash sparked a wave of public ire against financiers, and against rich people in general. It also intensified the debate about inequality, which has risen sharply in nearly all rich countries. In America, for example, in 1987 the top 1% of taxpayers received 12.3% of all pre-tax income. Twenty years later their share, at 23.5%, was nearly twice as large. The bottom half's share fell from 15.6% to 12.2% over the same period.



They don't do Dior here

Jan Pen, a Dutch economist who died last year, came up with a striking way to picture inequality. Imagine people's height being proportional to their income, so that someone with an average income is of average height. Now imagine that the entire adult population of America is walking past you in a single hour, in ascending order of income.

The first passers-by, the owners of loss-making businesses, are invisible: their heads are below ground. Then come the jobless and the working poor, who are midgets. After half an hour the strollers are still only waist-high, since America's median income is only half the mean. It takes nearly 45 minutes before normal-sized people appear. But then, in the final minutes, giants thunder by. With six minutes to go they are 12 feet tall. When the 400 highest earners walk by, right at the end, each is more than two miles tall.



The most common measure of inequality is the Gini coefficient. A score of zero means perfect equality: everyone earns the same. A score of one means that one person gets everything. America's Gini coefficient has risen from 0.34 in the 1980s to 0.38 in the mid-2000s. Germany's has risen from 0.26 to 0.3 and China's has jumped from 0.28 to 0.4 (see chart 2). In only one large country, Brazil, has the coefficient come down, from 0.59 to 0.55.

Surprisingly, over the same period global inequality has fallen, from 0.66 in the mid-1980s to 0.61 in the mid-2000s, according to Xavier Sala-i-Martin, an economist at Columbia University. This is because poorer countries, such as China, have grown faster than richer countries.

How much does inequality matter? A lot, say Richard Wilkinson and Kate Pickett, the authors of "The Spirit Level: Why Equality is Better for Everyone". Their book caused a stir in Britain by showing, with copious graphs and statistics, that inequality is associated with all manner of social ills. After comparing various unequal countries and American states with more equal ones, the authors concluded that greater inequality leads to more crime, higher infant mortality, fatter citizens, shorter lives, more teenage pregnancies, more discrimination against women and so on. They even found that more equal countries are more innovative, as measured by patents earned per person.

Mr Wilkinson and Ms Pickett suggest that equal societies fare better because humans evolved in small groups of hunter-gatherers who shared food. Modern, unequal societies are hugely stressful because they violate people's hard-wired sense of fairness. The authors call for stiffer taxes on the rich and more co-operative ownership of companies. Pundits on the left applaud, but others are not so sure.

Peter Saunders of Policy Exchange, a centre-right think-tank in London, thinks the book's statistical claims are mostly bunk. He points to several flaws. First, Mr Wilkinson and Ms Pickett did not exclude outliers from their sample. So, for example, when they say that unequal countries have higher murder rates than equal ones, all they have really observed is that Americans kill each other much more often than do people in other rich countries, perhaps because they are better armed. For the rest of the sample the link between inequality and homicide does not hold.

Likewise, their findings about life expectancy depend on the Japanese, whose longevity is more likely to be due to a healthy diet than to a flat income distribution. And their findings about teen births, women's status and innovation depend on Scandinavia, a region with a mild and sensible culture that is equally evident among people of Scandinavian stock who live in America.

Factors other than inequality are often more strongly correlated with the problems described in the book. In American states, for example, race is a far more accurate predictor of murder, imprisonment and infant-mortality rates, says Mr Saunders. He also chides the authors for ignoring countries that do not fit their theory, and for glossing over social problems, such as divorce and suicide, that are worse in more equal countries.

This debate will probably never be resolved. The statistical problems are tricky enough. If you measure inequality of wealth rather than income, the global pecking order changes. By this measure, Sweden is less equal than Britain, since fewer Swedes have private pensions. And if you measure consumption, the world seems a more equal place. The poor in rich countries often consume more than they earn, because they receive welfare benefits and use public services. The very rich often consume only a small portion of their income. Bill Gates is millions of times richer than the average person, but he does not eat millions of meals each day.

The philosophical questions are even trickier. It seems unfair that footballers, bankers and tycoons earn more money than they know what to do with whereas jobless folk and single parents struggle to pay the rent, notes Mr Saunders. Yet it also seems unfair to take money from those who have worked hard and give it to those who have not, or to take away the profits of those who have risked their life savings to bring a new invention to market in order to help those who have risked nothing. Different societies choose to deal with this conflict in different ways.

It is hard to gauge just how strongly people object to inequality. A recent poll by the BBC, a tax-funded broadcaster, found that many people in Britain think cashiers and care assistants should be paid more and chief executives and football stars less. Yet few Britons tip cashiers, boycott firms with fat-cat bosses or watch second-division football teams.

The Pew Global Attitudes Project asks people in various countries whether in their view "most people are better off in a free-market economy, even though some people are rich and some are poor." In Britain, France, Germany, Poland, America and even Sweden most people agree, but in Japan and Mexico most disagree. People in countries that have recently liberalised and are now booming are the most enthusiastic: 79% of Indians and 84% of Chinese say yes.

Degrees of fairness

Inequality jars less if the rich have earned their fortunes. Steve Jobs is a billionaire because people love Apple's products; J.K. Rowling's vault is stuffed with gold galleons because millions have bought her Harry Potter books. But people are more resentful when bankers are rewarded for failure, or when fortunes are made by rent-seeking rather than enterprise.

In the most corrupt countries the rulers simply help themselves to public money. In mature democracies power is abused in more subtle ways. In Japan, for example, retiring bureaucrats often take lucrative jobs at firms they used to regulate, a practice known as *amakudari* (literally "descent from heaven"). The Kyodo news agency reported last year that all 43 past and present heads of six non-profit organisations funded by government-run lottery revenues secured their jobs this way.

In America, too, ex-politicians often walk into cushy directorships when they retire. This may be because they are talented, driven individuals. But a study by Amy Hillman of Arizona State University finds that American firms in heavily regulated industries such as telecoms, drugs or gambling hire more ex-politicians as directors than firms in lightly regulated ones.

People from humble origins sometimes rise to the top. Barack Obama was raised by a single mother. Lloyd Blankfein, the boss of Goldman Sachs, is the son of a clerk. What such people usually have in common is uncommon intelligence.

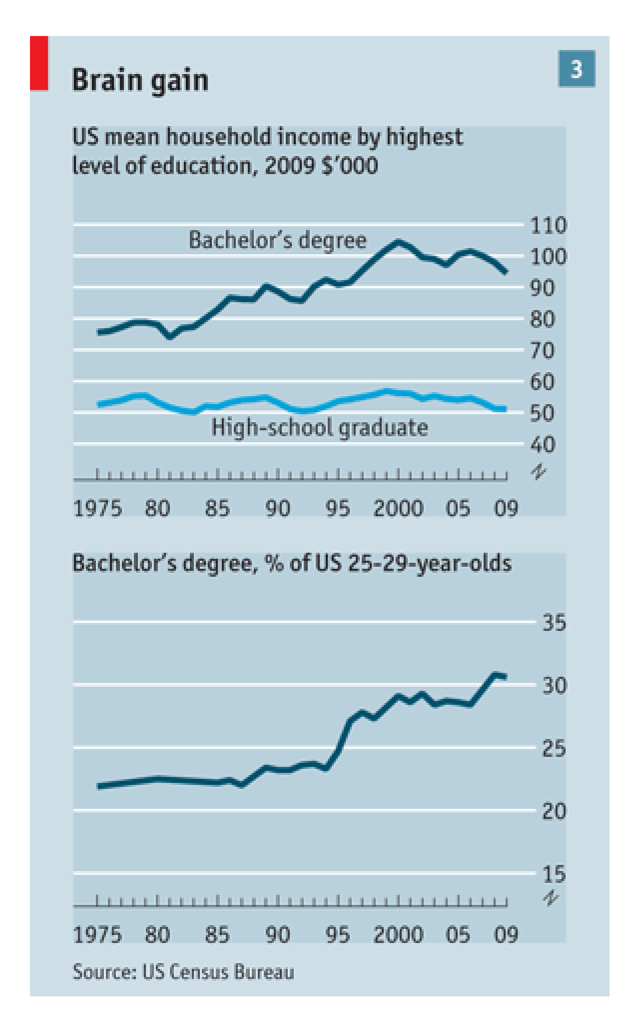
All kinds of talent are rewarded. But the number of people who get rich by singing or kicking a ball is tiny compared with the number who become wealthy or influential through brainpower. The most lucrative careers, such as law, medicine, technology and finance, all require above-average mental skills. A bond dealer need not appreciate Proust, but he must be

able to do sums in his head. A lawyer need not understand "A Brief History of Time", but she must be able to argue logically.

The clever shall inherit the earth

As technology advances, the rewards to cleverness increase. Computers have hugely increased the availability of information, raising the demand for those sharp enough to make sense of it. In 1991 the average wage for a male American worker with a bachelor's degree was 2.5 times that of a high-school drop-out; now the ratio is 3. Cognitive skills are at a premium, and they are unevenly distributed.

Parents who graduated from university are far more likely than non-graduates to raise children who also earn degrees. This is true in all countries, but more so in America and France than in Israel, Finland or South Korea, according to the OECD. Nature, nurture and politics all play a part.



Children may inherit a genetic predisposition to be intelligent. Their raw mental talents may then be nurtured better in some homes than others. Bookish parents read more to their children, use a larger vocabulary when they talk to them and prod them to do their homework. Educated parents typically earn more (see chart 3), so they can afford private schools or houses near good public ones. In America, where residential segregation is extreme, the best public schools are stuffed with college-bound strivers, whereas the worst need metal detectors. School reform helps, but cannot level the playing field.

"Assortative mating" further entrenches inequality. Highly educated men are much more likely to marry highly educated women than they were a generation ago. In 1970 only 9% of those with bachelors' degrees in America were women, so the vast majority of men with such degrees married women who lacked them. Now the numbers are roughly even (in fact women are earning more degrees) and people tend to pair up with mates of a similar educational background.

Women have made immense strides in the workplace, too. For example, in 1970, fewer than 5% of American lawyers were female. Now the figure is 34%, and nearly half of law students are female. So highly educated, double-income power couples have become far more common. The children of such couples have every advantage, but there are not many of them. The lifetime fertility rate for American high-school dropouts is 2.4; for women with advanced degrees, it is only 1.6. The opportunity costs of child-rearing are far higher for a woman who earns $200,000 a year than for one who greets customers at Wal-Mart. And raising elite children is expensive. A lawyer couple can easily afford to put one child through Yale, but perhaps not four.

The cost of higher education has contributed to plummeting birth rates among pushy parents in other rich countries, too. Greens may rejoice at anything that curbs population growth, but the implications of these trends are troubling. Demography makes it harder for people who start at the bottom of the ladder to climb up it. And that has political consequences.

A special report on global leaders

Not for sale

Jan 20th 2011 | from PRINT EDITION

Cash seldom buys political power. What counts are ideas and the ability to inspire



Silly signs win elections

THE popular view of politics is that it is all about money. This is an exaggeration. Consider the example of America, a country where government is often caricatured as "for sale". Rich candidates can buy a lot of airtime, which occasionally wins them office: think of Michael Bloomberg in New York. But often they flop: think of Mitt Romney, Steve Forbes, Ross Perot and Meg Whitman. Or John McCain, who alienated voters struggling with their mortgages when he could not recall how many houses he owned.

The American presidential election of 2008 cost more than $1 billion. That sounds a lot, but America has 300m people and dozens of television markets. Spending a shade over $3 per American to tell them about their presidential choices hardly seems excessive.

Barack Obama started with nothing, against an opponent, Hillary Clinton, who started with both money and connections. He ended up raising more cash because he inspired people. He ran a brilliantly decentralised campaign. Supporters set up 70,000 personal fund-raising pages, organised 200,000 campaign events and posted endless Obamaphile videos on

YouTube. Chris Hughes, a co-founder of Facebook, helped Mr Obama with the techie stuff. The Obama campaign showed how fast a web-savvy movement can spread.

The momentum did not last, however. With the economy still in a ditch, another popular movement eclipsed Mr Obama's. On February 19th 2009 a reporter called Rick Santelli lost his temper on live television. Reacting to the news of yet another bail-out for homeowners, he exploded: "The government is promoting bad behaviour!...This is America! How many people want to pay for your neighbour's mortgages that have an extra bathroom and can't pay their bills?" Mr Santelli called for a Tea Party: an anti-tax protest like the one in Boston that heralded the American revolution. The notion caught on. Tea parties erupted everywhere, attracting millions.

The Tea Party movement has a cranky fringe, but its core belief-that the government should tax and spend less-is attractive to many mainstream Americans. The tea partiers' passion helped Republicans to capture the House of Representatives last November.

Beautiful chaos

Technology has made it cheaper and easier for ordinary people to organise themselves. So the most influential political entrepreneurs are often those who can spot the next big thing and help it along. For example, an organisation called FreedomWorks, founded by Dick Armey, a veteran Republican and former House majority leader, offers tea partiers, many of whom are new to activism, practical tips on such things as setting up phone banks. Mr Armey makes no claim to lead the Tea Party movement. Adapting Hayek, he calls it "beautiful chaos...like the market".

The future of political activism lies in decentralisation, reckons Adam Brandon, a spokesman for FreedomWorks. His ideological opponents would agree. Ricken Patel, a Canadian activist, has built up a progressive campaigning group called Avaaz from nothing to 7m members in only four years, and on a trivial budget, by exploiting the power of the web.

Avaaz's dynamism is born of internal democracy: it adopts the issues its members tell it to adopt, from the humane (close Guantanamo) to the Luddite (ban genetically modified crops). Because it operates in 193 countries, it can turn local issues into global ones. It can muster a huge number of online signatures in a short time: its recent petition in defence of WikiLeaks collected 300,000 in 24 hours. It can make any politician's telephone ring off the hook.

The tea parties and Avaaz show that you do not need to spend a lot of money to be influential. Yet many groups and individuals try to translate cash into sway. Websites such as opensecrets.org publish a torrent of data showing how much American companies, industries and interest groups spend on lobbying and electioneering. The trend is relentlessly upward.

The amount spent on lobbying America's federal government has risen from $1.4 billion in 1998 to $3.5 billion in 2009. Spending on electioneering has shot up, too. In 2000 the total for all federal elections was $3.1 billion; in 2008 it was $5.3 billion. Elections in other countries are much cheaper. After adjusting for the difference in population, Britain's parliamentary poll last year cost only 7% of the American total, thanks to tight spending limits.

It is easier to count dollars than to measure their effect, however. Do rich donors decide elections? It is not clear that they do. For one thing, different donors often pursue different goals. George Soros, a progressive billionaire, backs progressive causes. The Koch brothers, two libertarian tycoons from Kansas, back libertarian ones. Corporations, too, are hardly monolithic. American oil firms tend to back Republicans. American lawyers (who give far more to campaigns) tend to back Democrats. Several industries, such as real estate and health care, back both sides.

In democracies with a free press, the main danger of money in politics is not that the rich will buy an election, but that they will lobby the victor for favours. A tax break here, a subsidy there and soon you are talking about real money. In America, lobbying by hospitals and drug firms soared as Congress debated Mr Obama's health reforms, which is perhaps why the bill that passed in 2010 was so porky. Worse, lobbying by coal firms has helped to stymie American action against global warming. But it was not the biggest obstacle to reform: voters hate high energy bills.

Politics in many countries is marred by nepotism. Even when elections are free, a candidate from a famous political family has a huge head start, in that voters already know his name. Americans have elected two presidents called George Bush. India has had three prime ministers from the Nehru-Gandhi clan, and may have more.

Yet the advantages of dynasty are diminishing. The internet helps talented newcomers to become famous fast. And voters often demand more than just pedigree, as Caroline Kennedy recently discovered when she tried to amble into a Senate seat.

One American senator in ten is closely related to another national politician, a ratio that has been falling steadily for two centuries. In the early days of the republic, it was closer to one in two.

The power of ideas

The strongest force shaping politics is not blood or money but ideas. The big movements of the past century-communism, fascism, democracy, liberalism-have all been propelled by big ideas, good and bad. So the people who influence government the most are often those who generate compelling ideas or supply them to the right politicians at the right time.

Edwin Feulner, for example, is one of the most influential conservatives in America. His face may be less familiar than Sarah Palin's, but his fingerprints can be found on the fine detail of legislation since 1977, when he took charge of the Heritage Foundation, a conservative think-tank. Heritage is big-it has a staff of 240 and more than 700,000 fee-paying members. And it is influential because it combines analytical rigour with shrewd marketing.

You need to define your target audience, says Mr Feulner. For him, that means Congress. Heritage's head office is a short walk from Capitol Hill, on the Senate side. Last year, to make it that little bit easier for members of the House of Representatives to pop in, Mr Feulner opened a second office on the House side. When a bill is being mooted, Heritage supplies ideas. During drafting, Heritage scholars suggest revisions. And when a vote is near, Heritage gives every lawmaker an easily digestible two-page document explaining what the bill contains and what its effects might be. Timing is crucial. "If you put an idea out too early, no one reads it. A day too late, you miss the vote," says Mr Feulner.

American think-tanks are more influential than those in other countries. They helped concoct the Marshall Plan and the Iraq war. They are often well funded. The Brookings Institution, a non-partisan outfit, has an annual budget of $80m. That is 25 times bigger than that of Demos, a rough British equivalent.

More importantly, American think-tanks are closely entwined with government. The president of Brookings, Strobe Talbott, was deputy secretary of state under Bill Clinton. John Podesta, the founder of the Centre for American Progress, a progressive think-tank, was President Clinton's chief of staff. Dozens of scholars from both institutions joined the Obama administration. A similar revolving door operates between conservative think-tanks and Republican administrations. The interchange creates lines of communication among wonks, lawmakers and the White House. Journalists talk to think-tankers because they know their ideas are taken seriously by those in power.

Debate among think-tankers is usually civil. Facts matter. Conservative and liberal wonks sometimes join forces to promote causes about which they agree. Heritage and Brookings, for example, have a joint venture called the "Fiscal Wake-Up Tour" to educate the public about America's unsustainable deficits.

Some accuse American think-tanks of an incestuous relationship with politicians, or of forming part of a permanent ruling class. There is some truth in this: think-tankers often stay inside the Beltway (the ring road around Washington, DC) all their working lives. But they are not impervious to elections. Liberal thinkers struggle to influence conservative administrations, and vice versa. And some think-tanks now operate on a global level, where parties matter less and ideas matter even more.

A special report on global leaders

The world's water-coolers

Jan 20th 2011 | from PRINT EDITION

Where the influential people meet and talk



Not everyone loves Davos

"YOU can do nothing against a conspiracy theory," sighs Etienne Davignon. He sits in a lofty office with a stupendous view over Brussels, puffing his pipe. He is an aristocrat, a former vice-president of the European Commission and a man who has sat on several corporate boards, but that is not why some people consider him too powerful. He presides over the Bilderberg group, an evil conspiracy bent on world domination. At least, that is what numerous websites allege; also that it has ties to al-Qaeda, is hiding the cure for cancer and wishes to merge the United States with Mexico.

In reality, Bilderberg is an annual conference for a few dozen of the world's most influential people. Last year Bill Gates and Larry Summers hobnobbed with the chairman of Deutsche Bank, the boss of Shell, the head of the World Food Programme and the prime minister of Spain. One or two journalists are invited each year, on condition that they abstain from writing about it. (Full disclosure: the editor of *The Economist* sometimes attends.)

Because the meetings are off the record, they are catnip to conspiracy theorists. But the attraction for participants is obvious. They can speak candidly, says Mr Davignon, without worrying how their words might play in tomorrow's headlines. So they find out what other influential people really think. Big ideas are debated frankly. Mr Davignon credits the meetings for helping to lay the groundwork for creating the euro. He recalls strong disagreement over Iraq: some participants favoured the invasion in 2003, some opposed it and some wanted it done differently. Last year the debate was about Europe's fiscal problems, and whether the euro would survive.

The world is a complicated place, with oceans of new information sloshing around. To run a multinational organisation, it helps if you have a rough idea of what is going on. It also helps to be on first-name terms with other globocrats. So the cosmopolitan elite-international financiers, bureaucrats, charity bosses and thinkers-constantly meet and talk. They flock to elite gatherings such as the World Economic Forum at Davos, the Trilateral Commission and the Boao meeting in China. They form clubs. Ethnic Indian entrepreneurs around the world join TiE (The Indus Enterprise). Movers and shakers in New York and Washington join the Council on Foreign Relations, where they can listen to the president of Turkey one week and the chief executive of Intel the next. The world's richest man, Carlos Slim, a Mexican telecoms tycoon, hosts an annual gathering of Latin American billionaires who cultivate each other while ostensibly discussing regional poverty.

Davos is perhaps the glitziest of these globocratic gatherings. Hundreds of big wheels descend on the Swiss ski resort each year. The lectures are interesting, but the big draw is the chance to talk to other powerful people in the corridors. Such chats sometimes yield results. In 1988 the prime ministers of Turkey and Greece met at Davos and signed a declaration that may have averted a war. In 1994 Shimon Peres, then Israel's foreign minister, and Yasser Arafat struck a deal over Gaza and Jericho. In 2003 Jack Straw, Britain's foreign secretary, had an informal meeting in his hotel suite with the president of Iran, a country with which Britain had no diplomatic ties. But Davos is hardly a secretive institution: it is crawling with journalists. The other globocratic shindigs are opening up, too. Even Bilderberg has recently started publishing lists of participants on its website.

Some American organisations, such as foreign-policy think-tanks, are also well placed to exert global influence. The Carnegie Endowment for International Peace, for example, has established itself as one of the most globally trusted talking-shops, with offices in Beijing, Beirut, Brussels and Moscow, as well as Washington-though it has yet to fulfil the vision of its founder, Andrew Carnegie, who wanted it to abolish war. The key to wielding influence, says Jessica Mathews, Carnegie's president, is "very simple. You hire the best people."

In countries where think-tanks are subservient to the state, such as China and Russia, foreign outfits such as Carnegie enjoy a reputation for independence. If they can back this up with useful knowledge, they can sway policy. For example, Carnegie scholars advised the authors of Russia's post-Soviet constitution. And when relations between American and Russia grew frosty under President George W. Bush, Carnegie's Moscow office helped keep a line of communication open between the two governments.

Such meetings are "an important part of the story of the superclass", says Mr Rothkopf, the author of the eponymous book. What they offer is access to "some of the world's most sequestered and elusive leaders". As such, they are one of "the informal mechanisms of [global] power".

Some globocrats think the importance of forums like Davos is overstated. Howard Stringer, the boss of Sony, is the kind of person you would expect to relish such gatherings. Welsh by birth, American by citizenship, he took over Japan's most admired company in 2005, when it was in serious trouble, and turned it around in the face of immense cultural obstacles. He says he has enjoyed trips to Davos in the past but will not attend this year. He can learn more, he says, by listening to his 167,000 employees.

On the face of it there seems much to be said for the world's shakers and movers meeting and talking frequently. Yet for all their tireless information-swapping, globocrats were caught napping by the financial crisis. Their networks of contacts did throw up a few warnings, but not enough to prompt timely action.

The limits of jaw-jaw

Jim Chanos, a hedge-fund manager who made his first fortune betting that Enron was overvalued, warned the G8 finance ministers in April 2007 that banks and insurance firms were heading for trouble. He made another fortune when bank shares crashed, but is still furious that his warnings were politely ignored. He thinks it an outrage that several senior regulators from that period are still in positions of power. And he accuses some bankers of "a wholesale looting of the system" by paying themselves bonuses based on what they must have known were phantom profits. He thinks they should be prosecuted.

Globocrats failed to avert the crisis, but they rallied once it struck. Rich-country governments acted in concert to prop up banks with taxpayers' money. In America the response was led by a well-connected trio: Hank Paulson, George Bush junior's treasury secretary and a former boss of Goldman Sachs; Tim Geithner, Barack Obama's treasury secretary and a former boss of the New York Federal Reserve, as well as a veteran of the IMF, the Council on Foreign Relations and Kissinger Associates; and Ben Bernanke, of Harvard, MIT, Stanford, Princeton and the Bush White House, who is now chairman of the Federal Reserve. The bail-outs were unpopular everywhere, but may have prevented the world's banking system from imploding.

Governments are now trying to craft rules to prevent a recurrence. Lots of people have offered advice. Among the weightier contributions was a report from the Group of Thirty (G30), an informal collection of past and present central-bank governors. The Volcker Report, advocating a central clearing mechanism for derivatives trading and curbs on proprietary trading by banks, helped shape America's Dodd-Frank financial-reform bill. The G30 is influential because it consists of people with experience of putting policies into practice, says Stuart Mackintosh, its director. So when it makes recommendations, they can be turned into action, he adds.

Index | A special report on global leaders

A special report on global leaders

The global campus

Jan 20th 2011 | from PRINT EDITION

The best universities now have worldwide reach

IT IS not just meetings of the rich and powerful that are getting increasingly cosmopolitan. Global universities are "reshaping the world", argues Ben Wildavsky, the author of "The Great Brain Race". Because big problems often transcend borders, many ambitious students demand a global education. The number of people studying outside their home country jumped from below 2m in 2000 to 3.3m in 2008, according to the OECD.

The most popular destination is the English-speaking world, led by America, which hosts 19% of the world's mobile students. French and German universities are also popular, but more narrow in their allure. Most of the foreign students in France come from Europe or former colonies in Africa, but foreign students in America come from everywhere.

America's lead is declining slightly, but remains huge at the top of the knowledge tree. Two-thirds of postgraduates who study abroad choose America. In some of the hardest disciplines most postgrads at American universities are foreign: 65% in computing and economics, 56% in physics and 55% in maths, notes Mr Wildavsky.

Feet on the ground

The best American universities are nothing like the stereotype of isolated ivory towers. Take the Massachusetts Institute of Technology (MIT), founded in 1861 to accelerate the industrialisation of America. Its ties with business are now intimate and global. Companies fund much of its research. Staff and students collaborate with established firms and set up a prodigious number of their own. A study in 2009 by the Kauffman Foundation, a think-tank in Missouri, estimated that MIT alumni had founded 25,800 companies that were still active, employing 3.3m people and generating annual sales of $2 trillion. "It's a very entrepreneurial culture," says Susan Hockfield, MIT's president.

The university gets buckets of cash from the government, but Ms Hockfield does not like to rely on it. A new energy-research initiative was funded with more than $300m from private companies such as Eni, an Italian energy firm, and ABB, a Swiss-Swedish industrial conglomerate.

Ms Hockfield, a neuroscientist, is excited by the potential of collaboration across disciplines. In the 20th century technological progress was driven by the convergence of engineering and physics, which yielded electronics. In the 21st century the hot area will be the convergence of engineering and biology, she predicts. For example, MIT's cancer-research centre is staffed by a mix of biologists and engineers. Its projects include making nanoparticles that can destroy cancer cells. Another team at MIT, led by Angela Belcher, has found a way to make genetically modified viruses synthesise the cathodes and anodes of lithium-ion batteries at room temperature. This saves energy and uses no harmful organic solvents.

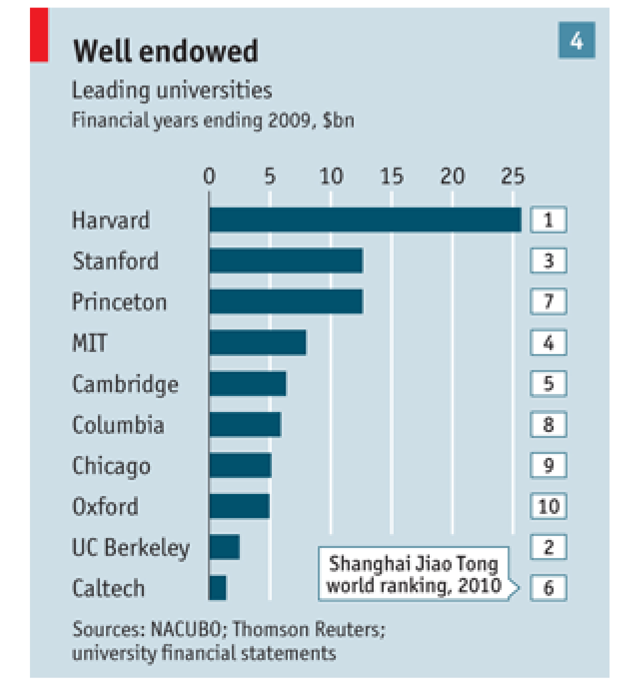
As well as generating knowledge, MIT spreads it. It does so both in narrowly targeted ways, such as advising the White House, and in scattershot ways, such as posting its course materials on the internet. Nearly everything, from texts to videos of lectures, is available online free. You can read the simplified "Highlights for High School" or walk yourself through a whole course, says Ms Hockfield. Since the service began in 2002, some 70m people have used it-roughly 7,000 times the number of students currently attending MIT.

The university promotes collaboration across borders, too. It finds internships abroad for its students and operates a raft of joint ventures, working with foreign academics to improve urban planning in China and poverty relief in India.

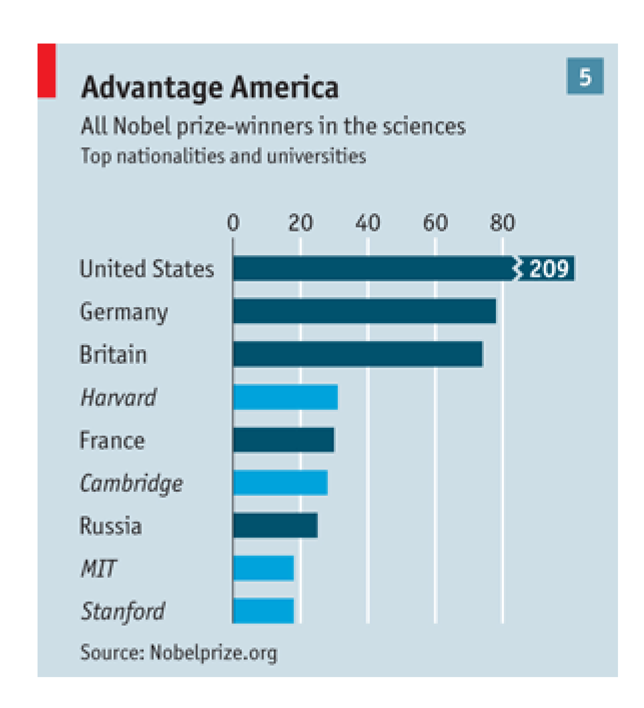
"All the interesting problems cross boundaries," says David Ellwood, the dean of Harvard's Kennedy School of Government. Some straddle borders. Some straddle disciplines. Some require co-operation between business, government, academia and non-profit groups. "So you have to train people to cross boundaries," Mr Ellwood concludes.

Leaders need "an incredible curiosity" and a capacity to listen, he says. At Harvard they hear a range of views on the appropriate relationship between governments, markets and citizens. Students are exposed to arguments for and against democracy. They see the problems associated with quick election cycles and extreme partisanship, notes Mr Ellwood, but also the benefits of accountability. For students who plan to go home and run China, that may matter some day.

Nearly half of the Kennedy School's students are foreign. Alumni include the secretary-general of the UN, the president of the World Bank, the head of China's Organisation Department (China's top civil servant), the prime minister of Singapore and the current presidents of Mexico, Mongolia, Liberia and Colombia-as well as Klaus Schwab, the founder of the World Economic Forum.



The world's best universities recruit from a global talent pool for both students and staff. This not only enhances their academic firepower but also makes their alumni part of a global network. A graduate of France's Ecole Nationale d'Administration can find fellow *enarques* in every part of the French establishment. A Stanford graduate can find other influential Stanford graduates anywhere in the world.



By a popular Chinese ranking, compiled by Shanghai's Jiao Tong University, 17 of the world's leading 20 universities are American. Lots of them are very rich (see chart 4). They also win a disproportionate share of Nobel prizes (see chart 5). This is an important source of soft power for America. Its government may no longer inspire as much respect or fear as it once did, but a disproportionate share of global leaders are American-educated, so they are familiar with American values.

Some people find the growing influence of globally educated elites alarming. The late Samuel Huntington, a Harvard professor who became famous for his 1996 book "The Clash of Civilizations and the Remaking of World Order", fretted that globocrats have "little need for national loyalty" and see national governments as relics "whose only useful function is to facilitate the elite's global operations". That may be true of a few, but ethnic and national loyalties remain strong.

Index | A special report on global leaders

A special report on global leaders

Crazy-talking boffins

The surest way to wield influence is to invent something useful


No idea is too wacky for Mr Myhrvold

WHEN trying to generate new ideas, "you have to make sure people feel OK about saying crazy things," says Nathan Myhrvold. His firm, Intellectual Ventures, seeks to profit from inventions. Mr Myhrvold does not need the money; as a former chief technology officer of Microsoft he already has sacks of it. But he believes that "invention is the closest thing to magic we have."

Mr Myhrvold convenes "invention sessions", each one including thinkers from a variety of fields. He puts them in a room with gallons of coffee and lets them bounce ideas around. Assistants record the conversation and jolly it along by projecting relevant scientific papers onto a screen. Mr Myhrvold, a physicist by training, takes part with gusto.

Because he is brainy and well connected (investors in his firm include Microsoft, Intel, Apple, Google, Sony and Nokia), other brainy people are happy to attend his pow-wows. No idea is too outrageous to receive a hearing. One participant suggested killing malarial mosquitoes with laser beams. Everyone laughed. But then they started thinking about it and realised that laser technology is much cheaper than it was, thanks to Blu-Ray players and laser printers. A working prototype was built in 2008. The firm is now looking for a partner to manufacture it.

Among other things, his team has designed a nuclear reactor that would use nuclear waste as its fuel. This, he says, would squeeze 20 times more power out of uranium than current technology does. He and Bill Gates set up TerraPower, an energy firm, to develop the idea. This is the kind of ambitious and risky bet that the world has to make if global warming is to be curbed, says Mr Myhrvold. If it comes off, he will make another fortune. If not, he has plenty of other ideas.

Mr Myhrvold's firm illustrates some useful principles for those who want to foster innovation. First, as technology grows more complex, advances depend less on individual inspiration and more on collaboration. The more that the millions of scientists in the world talk to each other, the more good ideas will emerge. The number of patents granted has risen from 900,000 in 1985 to 1.9m in 2008.

Mr Myhrvold's firm is based near Seattle, but flies in scientists from far and wide and maintains a subsidiary in India to tap the torrent of innovation there. Its boffins in Bangalore are working on projects ranging from a red laser to preserve food to a DNA nano-machine to deliver drugs to precisely the right spot in a patient's body.

The second principle is that profits matter. Invention has many mothers, of which money is probably not the most important. Inventors tinker because that is what they love doing. Necessity, famously, plays a role. But inventors also

want to live well. The profit motive is a crucial source of discipline. It is one thing to make a battery-powered car; quite another to make one sufficiently cheap and powerful for people to buy it.

Yet the market for ideas is far from perfect. Capital is impatient. There is plenty of venture capital for ideas that promise returns in the short or medium term, but longer-term research and development depends heavily on governments. It is typically funded on a charitable basis: "Give me the money and you'll never see it again," as Mr Myhrvold puts it. He favours a more businesslike approach, involving a more liquid market for investors to buy and sell ideas. Such a market, he thinks, would attract billions of dollars for new inventions.

His ideas are controversial. Intellectual Ventures, as well as generating its own ideas, buys sheaves of patents from others. Some people in Silicon Valley fear that Mr Myhrvold will use his portfolio of patents to sue technology firms for allegedly infringing them. But Mr Myhrvold denies any intention of becoming what Valley folk call a "patent troll". He runs a number of funds that allow patient investors to take a punt on a basket of ideas that may produce a long-term pay-off. This generates immediate rewards for inventors who sell their patents, thereby encouraging innovation, he argues.

Index | A special report on global leaders

A special report on global leaders

Tribes still matter

Jan 20th 2011 | from PRINT EDITION

How global leaders tap into diaspora networks

HUNDREDS of millions of Indians cannot prove they exist. They have no birth certificate, no driving licence, no social-security number. So they find it hard to open a bank account, borrow money or draw on government services.

Nandan Nilekani, an Indian software billionaire, volunteered to give every one of his 1.2 billion compatriots an identity number tied to biometric data. The Indian government thought this a wonderful idea, but there was a snag. The proposed database was ten times larger than the largest biometric database in existence. How was a poor country going to build it?

Mr Nilekani turned to the Indian diaspora for help. He called up ethnic Indians who had done well in Silicon Valley. Before long they were calling their friends and urging them to join in. The overseas Indians brought oodles of useful experience. Raj Mashruwala had helped to set up the number-crunching system for the New York Stock Exchange. Srikanth Nadhamuni had helped set up Healtheon, a big health IT firm. The team assembled in Bangalore, set up a whiteboard in a rented apartment and started brainstorming.

The programme went from start-up to roll-out in little more than a year, with the first identity numbers allocated in October 2010. If everything works as planned, poor Indians will for the first time be able to prove who they are, thus making themselves more creditworthy.

Mr Nadhamuni thinks all sorts of services can be grafted onto the national ID system. A migrant labourer with no bank account will be able to wire money to his mother by sending it to her ID number. His mother will be able to pick up the cash at her local village shop, which will have a miniature scanner for her fingerprints. The shopkeeper will charge a small fee for the service. Villagers will no longer have to waste days trekking to the nearest town to get to a bank.

Brainy globetrotters are rarely rootless. Even the most cosmopolitan usually feel an affinity with others who share the same language, culture or heritage. That is why diaspora networks are so powerful, and why some of the world's most influential people rely on them so heavily.

Some diasporas are vast and global. For example, there are an estimated 25m non-resident Indians and 60m overseas Chinese, including significant numbers in nearly all countries. They create a web of cross-border connections. Boffins are 30-50% more likely to cite a paper by someone of their own ethnicity than you would expect if such ties made no

difference, according to William Kerr of Harvard Business School. Diaspora networks speed the flow of information, the lifeblood of science and commerce.

They also foster trust. A Lebanese trader in west Africa will feel safe doing business with a Lebanese trader in Latin America because one man's high-school friend knows the family of the other's wife back in Beirut. That means they can seal big deals with a single phone call. If one cheats the other, he will be shut out of the entire Lebanese diaspora trading network.



Yes, it's me. Now lend me some money

World wide web of migrants

Networks of exiles dominate trade in many parts of the world: the Indians in east Africa and parts of the Caribbean, the Chinese in South-East Asia, and so on. A disproportionate number of prominent businesspeople come from migrant families. Carlos Slim, the world's richest man, is Lebanese-Mexican. Mukesh Ambani, India's richest man, was born in what is now Yemen. Eric Li and Robin Xu, the founders of Baidu, China's answer to Google, used to work in America.

Migrants form bridges between the countries they live in and the ones they hail from. This is especially true of the overseas Chinese (including those in Hong Kong and Taiwan), who handle some 70% of foreign direct investment into China. They have three advantages: they speak the language, they understand the culture and they have *guanxi* (connections).

Mei Xu, a Chinese-American entrepreneur, left China after the Tiananmen Square massacre. She was a student in Beijing, which in the government's eyes made her a potential agitator for democracy. So she was sent to do a dull job in a warehouse in the middle of nowhere. She emigrated to America, yet retained her contacts in China. With her husband, David Wang, she started a business. She asked her friends in China to help her find Chinese products that might sell well in America, and settled on arty scented candles. In 1995 she persuaded her sister to open a factory in Hangzhou to supply them.

The candles proved popular. Target, a chain store, ordered $2m worth, then quadrupled the order. The factory could not cope. With only two months to meet the Christmas rush, Ms Xu had to find extra capacity somewhere in China. She succeeded, with no time to spare, by calling all her contacts. "Someone who does not know China could not have done that," she says. Her firm, Pacific Trade International, now generates about $100m in annual sales.

Even a relatively low-tech business such as candle-making evolves rapidly. Ms Xu's supply chain is now multinational. The most imaginative designs are created in America. Routine design work is done in China. The candles are mostly made in Vietnam. The firm also has a factory in Maryland to satisfy its most impatient customers. China is no longer just a source of cheap labour, says Ms Xu. It is a blossoming market and increasingly a source of new ideas.

Studies of business leaders tend to emphasise their vision, drive and ruthlessness. Such traits are important, but members of the global elite are human, too. Sajjid Chinoy, an economist at JPMorgan in Mumbai, returned to India after living in America for 15 years. An outsider might have thought that he moved back because India's economy is growing much

faster than America's, creating boundless opportunities for bright young brainworkers. In fact, he returned because his brother had been injured in a terrible car accident. "It's often about family," he says.

A special report on global leaders

Asia's new aristocrats

Jan 20th 2011 | from PRINT EDITION

What Indians and Chinese make of their tycoons



Costly cars for comrades

A TINY tropical fish sits in a glass vase on each table in a restaurant in the lobby of the Oberoi Hotel. A bright red piano fills the air with music. The passion fruit souffle with bitter chocolate pave and goats' milk ice cream is delicious. The bill would ruin most Indians.

One day gunmen walked into the restaurant and shot diners and staff at close range, spattering blood over the walls. At least 175 people died in the attacks that began on November 26th 2008 in Mumbai. The terrorists appear to have chosen their targets precisely. A crowded station, to maximise the death toll. A small Jewish centre. And the poshest hotels in Mumbai-the Taj and the Oberoi-which were packed with the city's elite.

"Everyone in my social class lost friends," says Cyrus Guzder, the chairman of AFL, a logistics firm. "We all socialise at the Taj and the Oberoi. We've all been to weddings and parties here." He sits in a soft chair in a members-only club in the Oberoi as a waiter serves canapes. The club is quiet and uncrowded, a rare luxury in this heaving, bustling city of 14m.

India's movers and shakers all seem to know each other. The Indian elite have created their own islands, frowns a cabinet minister: "It's a bit unhealthy." They send their kids to private schools. They have their own water and electricity. So they barely notice how bad the government is at delivering power, water and schooling to the other 1.2 billion Indians.

Yet to many Indians the nation's tycoons are heroes. A few made their fortunes corruptly, but the software moguls of Bangalore created a huge export industry out of nothing, and many others helped to spur India's galloping growth. Ratan Tata, the soon-to-retire boss of a conglomerate that produces everything from tea to cars, lives modestly and treats his

employees well. The brothers Anil and Mukesh Ambani are more controversial, but they have turned the family business into two global giants, with interests from chemicals to entertainment.

Some Indian gazillionaires are flashy. Mukesh Ambani's house has 27 stories, three helipads and three floors of hanging gardens. Vijay Mallya, a beer-and-airlines magnate, constantly amuses the newspaper-reading public with his speedboats and sports teams. But for most of the country's elite the most conspicuous item of consumption is sending their children to university in America.

In much of India, life is getting perceptibly better each year. Wealth per person has vaulted by 150% in the past decade, from $2,000 to $5,000. Many Indians think the nation's entrepreneurs deserve some of the credit. In Dharavi, a slum outside Mumbai, an illiterate mother called Aruna sits in her tiny one-room flat, which is home to ten people. Asked how she feels about the rich, she says: "They have worked hard. And we must work hard, too." Her eldest daughter has a job entering data at a bank. The next one is studying diligently. The family may be near the bottom of the ladder, but it sees a way up.

The party is watching you

The relationship between rich and poor in China is different. China's stellar growth has lifted some 500m people out of poverty. Much of the credit belongs to Chinese entrepreneurs. Since Mao's boot was lifted from their necks, they have built marvels, from the skyscrapers of Shanghai to the factories of Guangdong. Yet mainland Chinese business leaders operate in the shadow of a secretive and unaccountable ruling party. To get on, many join it. Some do so reluctantly, to avoid being crushed. Others do so gladly, hoping to use the power of the state to enrich themselves.

Individual party members are not entirely above the law. If a local bigwig behaves so appallingly that the resulting protests are heard in Beijing, the party may cut him down to size. In October last year the son of Li Gang, a senior police officer in Baoding, killed a pedestrian while allegedly drink-driving. He sped off, shouting, "report me if you dare; my dad is Li Gang!"

News of the incident went viral in the Chinese blogosphere. Pop songs with the refrain "My dad is Li Gang!" quickly circulated. Li Gang was forced to make a televised apology. His son was arrested. China's leaders would like the 95% of the population who are not members to think that the party cares. But the most revealing fact is that Mr Li junior evidently thought he could get away it.

The party's tentacles are everywhere. State-owned firms do its bidding. Private firms must avoid offending it. Projects it supports make rapid progress. For example, it wants China to dominate the market for green energy. So when the price of polycrystalline silicon (the main raw material for solar panels) shot up in 2007-08, a businessman, Zhu Gongshan, won swift approval to build a factory to make it, and China's sovereign-wealth fund invested $710m in his venture.

But since the party is accountable neither to voters nor to the law, there is little to prevent its bosses from abusing their power. The children of some of China's leaders have amassed huge fortunes in murky ways. Banks often lend to the well-connected instead of the creditworthy. Local leaders levy taxes that have no basis in law.

Because business and power are so entwined, even the most able businesspeople are treated with suspicion outside China. For example, Huawei, a maker of telecoms equipment, whose products are generally considered excellent, nevertheless has trouble doing business in America because its founder, Ren Zhengfei, is a retired army officer. Some American congressmen assume that Huawei is a front for the People's Liberation Army. They fear that if the firm is allowed to supply sensitive communications infrastructure, it might bug it so that China's spies can listen in. There is no evidence to support this idea, but no way to investigate it either: Huawei's ownership structure is opaque.

The perception that commercial success often depends on political ties makes inequality in China more galling. In the mid-1980s Chinese incomes were more evenly distributed than India's-hardly surprising, since China was nominally communist and India is afflicted by a caste system. But now China is less equal than India, with a Gini coefficient of 0.4 to India's 0.37. China has 800,000 dollar millionaires, but also 400m people who live on less than $2 a day.

The disparity between rural and urban incomes is also vast. City-dwellers make two-and-a-half times as much as rural Chinese-the widest such gap in any big country. This is partly because of a system of residence permits, called *hukou*, that resembles the pass system in South Africa under apartheid. People with a city *hukou* can live and work there freely. Those with a rural *hukou* can come to a city only as guest workers. Some 150m rural Chinese work in cities without the right to live there, in effect making them foreigners in their own country. They often cannot use public schools and clinics, and they are barred from public housing. Peasants who protest can be deported back to the countryside.

The government has promised to liberalise the *hukou* system, but cities can still exclude anyone they like, and often do. Real freedom of movement would prompt 250m peasants to move to the cities, predicts Yukon Huang, a former head of the World Bank's office in China. City folk don't want that. The incomers might clog their schools, build slums on their doorstep or compete with them for jobs.

Or for women. Guy Sorman, the author of a sceptical book about China, "The Empire of Lies", describes a rule in Shanghai that allows a local man to obtain a *hukou* for his wife from outside after 15 years of marriage, but makes no provision for a Shanghai woman to marry someone from elsewhere. Asked why not, the mayor's office told Mr Sorman it was unthinkable that a Shanghai woman would marry a "foreigner".

The *hukou* system was designed to help the party control the people. But by creating two Chinas, it is building up tensions that one day could explode.

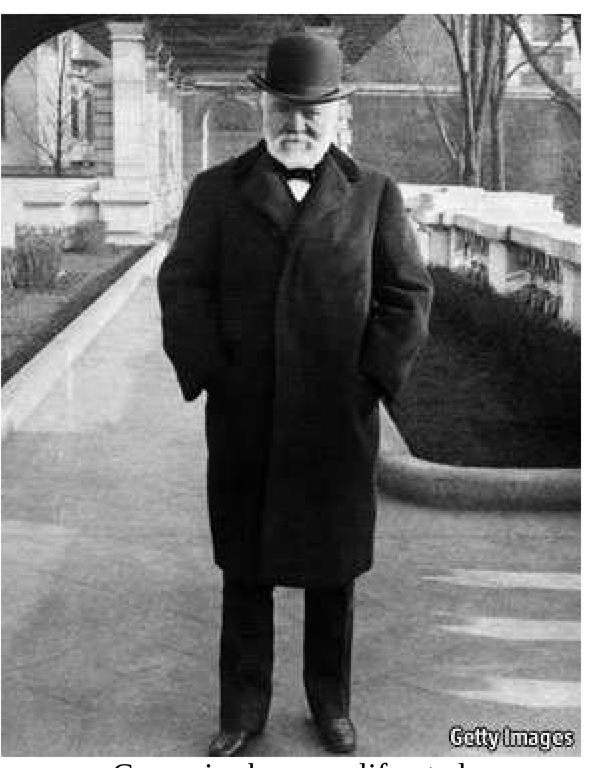
Index | A special report on global leaders

A special report on global leaders

They work for us

Jan 20th 2011 | from PRINT EDITION

In democracies the elites serve the masses



Carnegies have proliferated

IN SEPTEMBER last year Bill Gates and Warren Buffett sat down with 50 of China's richest tycoons to a sumptuous dinner of nothing at all. The point the two philanthropists were making was that those who have more money than they can ever spend on themselves should consider spending it on others.

Philanthropy has a long history. What is new is that philanthropists now have more money to give away than ever before. They are often young, energetic and intellectually gifted, too. Bill Gates was only 39 when he set up his charitable foundation, so he could end up spending more years managing his charity than he did running Microsoft. Mark Zuckerberg, the founder of Facebook, was only 26 when he gave $100m to schools in Newark.

Modern philanthropists are typically self-made, so they are used to getting things done. Rather than simply handing sacks of cash to charities that already exist, they often prefer to build their own institutions, observes Paul Schervish, the director of Boston College's Centre on Wealth and Philanthropy. The way they measure their success is not by how much they disburse but by the return they earn on their charitable investment, measured in lives saved or improved.

The super-rich philanthropists of a century ago, such as John D. Rockefeller and Andrew Carnegie, were equally driven but less numerous. Today there are well over 400 billionaires in America alone, many of them in fine fettle and eager to embark on a second career. Such people are often workaholics and have no wish to retire.

The charitable rich do their bit to soothe the social tensions that arise from growing inequality. Yet their work should be seen in perspective. Even in America voluntary transfers of wealth are dwarfed by public spending. Americans gave away $217 billion in 2009, estimates Mr Schervish. Government spending on health care and pensions was ten times that.

By and large, global leaders change the world more by doing their day jobs than in their spare time. Even Mr Gates, who was widely reviled for his business activities, probably did more good by amassing his fortune than he is doing by giving it away. The computer revolution he helped to bring about transformed the way people handle information. Perhaps his foundation will spur some equally momentous change, but it seems unlikely.

Tying Gulliver down

Recent history bristles with examples of the elite causing mischief. In 2008 clever but reckless bankers sparked a global meltdown. Governments are quite rightly taking steps to rein in their excesses; tougher regulations may reduce the risk of a repeat, but will not eliminate it. On a smaller scale, the world's brainy citizens are not necessarily being altruistic even when they claim to act for the common good. American lawyers, in punishing doctors' mistakes, make medicine more costly. Students in Europe riot to demand that others, including those not fortunate enough to attend university, pay for their tuition.

The elite are most likely to do harm when they rely on the coercive power of the state: for example, when they persuade it to grant them special favours. In autocratic countries such as China and Russia the most influential people devote a disproportionate amount of energy to such rent-seeking. In liberal democracies ordinary folk are better defended. Elections force politicians to take the public's wishes into account every few years. Competitive markets force business leaders to heed their customers' demands all the time. And the law applies to rich and poor alike, even if the rich can afford better lawyers.

All these curbs require continual refinement: greater transparency in government, vigorous enforcement of antitrust rules, efforts to make justice swift and fair. Yet by and large in liberal democracies the powerful get on by pleasing others. In short, they work for us.

Index | A special report on global leaders

A special report on global leaders

Sources and acknowledgments

Jan 20th 2011 | from PRINT EDITION

Besides those mentioned in the text, the author would like to thank: Paul Adamson, Andrew Belfer, Steve Braverman, Dick Costolo, Clive Crook, Sulaiman al-Hattlan, Mazen Hayek, Kathrin Hille, Jonathan Hova, Ronald Howes, Mishal Kanoo, Jonathan Kempner, Glenn Hubbard, Andrew Likierman, Iyad Males, Ed Merchant, Arif Naqvi, Ahmed Nassef, Sooud al-Qassemi, Jesse Scott, Michael Sonnenfeldt, Miles Varn, Evan Williams, Tarik Youssef, and several others who must remain nameless.

Sources include:

Global Wealth Report 2010, Credit Suisse

World Wealth Report 2010, Capgemini/ Merrill Lynch

"Richistan: A Journey Through the American Wealth Boom and the Lives of the New Rich". By Robert Frank.

"Superclass: The Global Power Elite and the World They Are Making". By David Rothkopf

"Fool's Gold: How Unrestrained Greed Corrupted a Dream, Shattered Global Markets and Unleashed a Catastrophe". By Gillian Tett

"The Great Brain Race: How Global Universities are Reshaping the World". By Ben Wildavsky

"The Spirit Level: Why Equality is Better for Everyone". By Richard Wilkinson and Kate Pickett

"Beware False Prophets: Equality, the Good Society and the Spirit Level". By Peter Saunders

"The Party: The Secret World of China's Communist Rulers". By Richard McGregor

"The Empire of Lies: The Truth About China in the 21st Century". By Guy Sorman

---

A special report on global leaders

Offer to readers

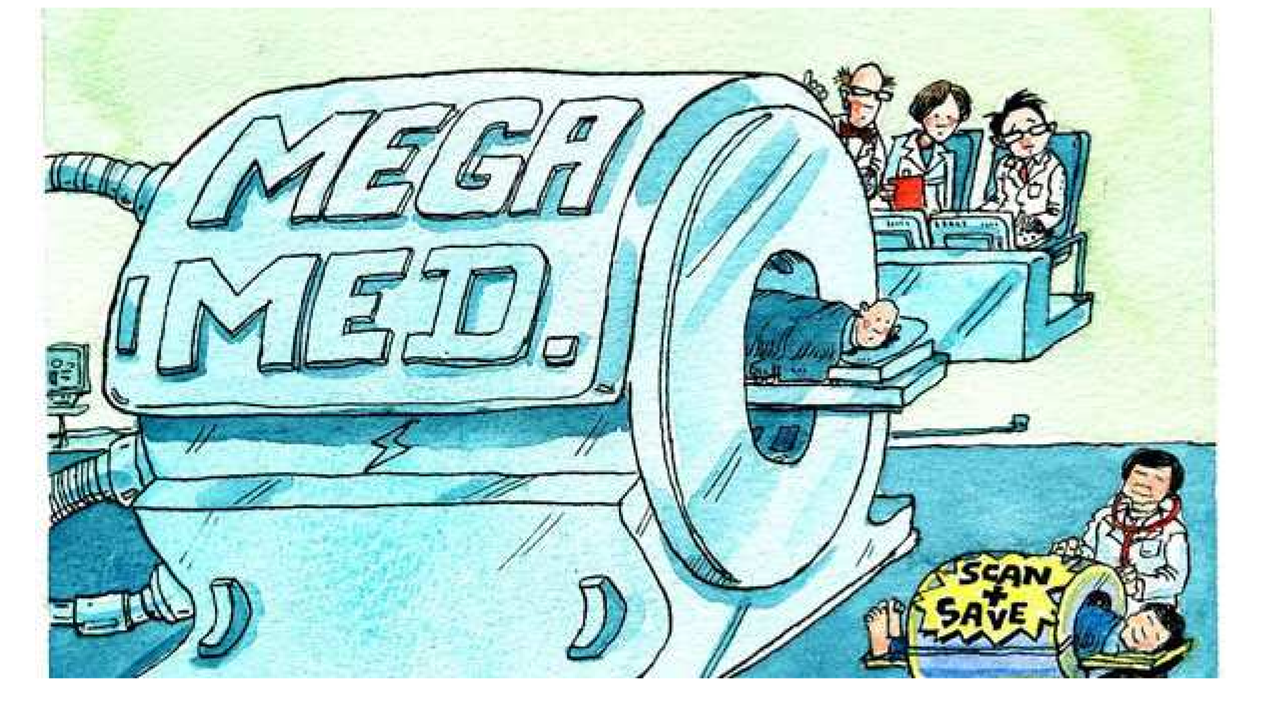
Jan 20th 2011 | from PRINT EDITION

Medical technology

Frugal healing

Jan 20th 2011 | *BEIJING* | from PRINT EDITION

Inexpensive Asian innovation will transform the market for medical devices

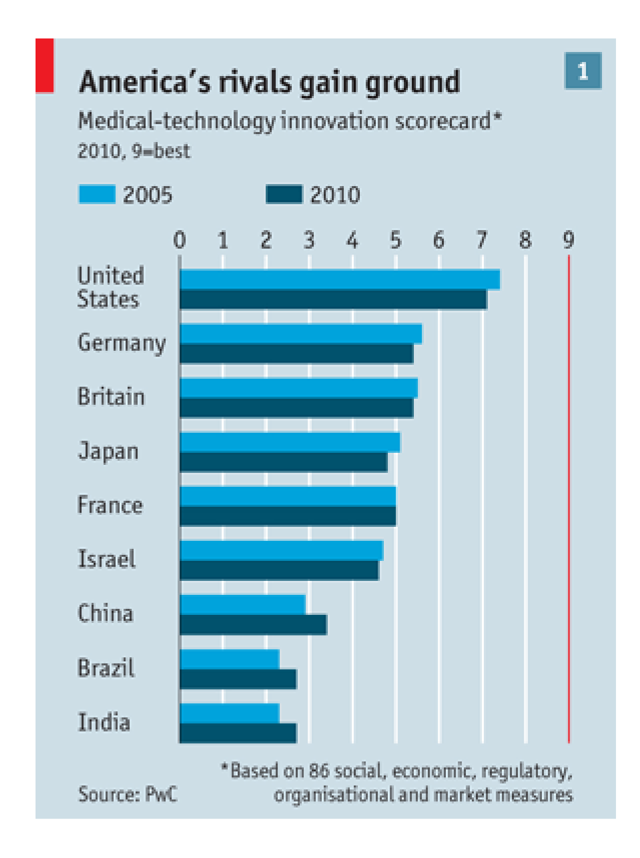


NINETY minutes north-east of Beijing lies what may be the future of medical technology. Weigao, a Chinese firm that started as a state-owned "township enterprise", has built a research and manufacturing centre where the laboratories are surprisingly chilly. Only the clean room, it seems, is fully climate-controlled. And that offers a lesson about frugal innovation. Whereas Western technology firms have plush premises, in China the people shiver while fancy equipment stays warm.

Though cold, Weigao's labs are a steaming cauldron of creativity. Medtronic, a giant American maker of medical devices, entered a joint venture with the Chinese firm two years ago. Its designers and engineers work side by side with local talent, and have already launched half a dozen inexpensive, novel products that Medtronic would not have made on its own.

This is new territory for Medtronic, which has hitherto made high-end, costly kit. Simon Li, the well-connected head of the joint venture, says that three things persuaded the American firm to see China "not as a host but as a home".

First, local demand: as China's second-tier cities boom, their clinics are crying out for cheap gizmos. Second, the Chinese government is pushing "indigenous innovation" by favouring local firms in tendering, procurement and so on. An engineer gleefully points out that as a local entity the Medtronic joint venture can buy essential rare-earth metals cheaply, despite Chinese restrictions on their sale (see article). Third and most important, Medtronic "just had to localise", says Mr Li, because it faced sudden and intense competition from local rivals.



A decade ago America's medical-technology firms dwarfed all others and China's were barely visible. But according to PwC, a consultancy, America's lead will shrink over the next decade on all important measures of innovation (see chart 1). China could well become a bigger force in this market than Europe by 2020-both by creating new medical technology and by using it.

Take sutures (for closing wounds), for example. The old approach was to make disposable ones and sell lots of them. But Chris Wasden of PwC notes that Chinese firms have undercut Western rivals by developing reusable ones.

The market for heart stents is another straw in the wind. Seven years ago, says Mr Li, Western firms like his thought their dominance was secure. When MicroPort, a Chinese upstart, came out with products that were 40% cheaper, he recalls, doctors were initially sceptical. But it did hundreds of clinical trials and now it owns 70% of the Chinese market, he notes.

Similar tales are legion. Investors have noticed. MicroPort and Lepu Medical, a local rival in the stent market, have both had successful public placements (the former in Hong Kong, the latter in Shenzhen). Trauson, a Chinese firm specialising in orthopaedics, listed last year in Hong Kong. Mindray Medical, a New York-listed Chinese firm that makes cheap monitors, exports lots of them to rich countries.

Sales of medical technology are exploding. The market in China is forecast to grow by 15% a year to 2015, reaching $43 billion by 2019; India's is galloping at 23%, and should top $10 billion by the decade's end. The Chinese government plans to spend $125 billion over three years to expand health care outside the biggest cities. That should boost demand even more.

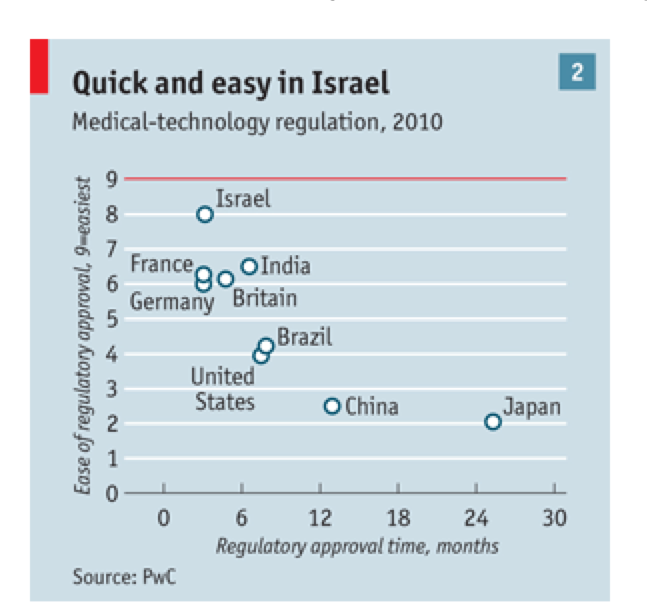
There are two Chinas: one fancy, one frugal. Ronald de Jong of Philips, a Dutch multinational, reveals that his firm sold more high-end CT scanners in China last year than it did in America. But mindful of China's big push to extend health care into rural areas, Philips has also made numerous local acquisitions. He says the chief benefit is access not to cheap labour but rather "to a culture of frugality".

Omar Ishrak of GE argues that the term "frugal innovation" understates the revolution under way, in which price is only one element. In designing new products, firms in emerging markets are leapfrogging to the latest technologies, such as miniaturisation, mobile communications and advanced materials. That enables them to build devices that are both cheaper and better than rich-country models. He cites the example of Brivo, a locally developed line of MRI and CT scanners.

All very impressive. But Chinese firms are not going to take over the medical-technology market just yet. They are good at making relatively simple devices and strong in non-invasive fields such as imaging, but they have yet to penetrate risky and sophisticated markets such as those for implanted defibrillators, says Rajesh Parekh of McKinsey, a firm of consultants.

What is more, says Rachel Lee of the Boston Consulting Group, the in-country laboratories set up by foreign firms are doing better at cutting-edge research than are their local rivals, which are focused on development. That suggests that Western firms still have a few years to master frugal innovation-and import it to their home countries-before the Asians arrive.

Several Western firms insist that this is precisely what they are already doing. They trot out a few colourful examples of frugal products they offer in rich countries. But careful scrutiny reveals that such examples are rare.



A disarmingly honest Mr Ishrak of GE explains that America's risk-averse regulators (see chart 2) and its complex systems of financing health care are a problem, but he adds that "manufacturers are also to blame." The sales and distribution systems at firms like his, set up to sell $100,000 scanners, are ill-suited to sell versions at a tenth of that price. Also, he confesses, makers "do not present comprehensive evidence of value"; rather, he thinks, they rely on "an emotional kind of sale".

That may have worked in the past, but as health budgets are squeezed in the West and cheaper technologies emerge from the east, emotion will surely yield to economics. The only question left is whether the frugal innovators who come out on top will use forks or chopsticks.

Japan responds to China

Rare action

Jan 20th 2011 | *TOKYO* | from PRINT EDITION

Corporate Japan adjusts quickly to a shortage of rare earths



No rare earths, no mobile phones

TWO decades of economic impotence have convinced many observers that Japan is cautious and slow to change. But the country can move quickly when sufficiently provoked. China is hoarding rare earths-17 elements that, although plentiful in nature, are costly and time-consuming to extract and have highly toxic by-products. Four months ago, during a minor territorial dispute, China was accused of suspending shipments of these elements to Japan entirely. Since then, Japan Inc has sprung into action.

Rare earths are used in high-tech products from computer chips and televisions to cars and missiles. China has one-third of the world's reserves but accounts for 97% of current production, having squeezed out other suppliers with low prices in the 1990s. It is restricting exports to induce foreign technology firms to place operations inside China. The quota for January to June this year was cut by 35%.

Japan imports more rare earths than any other country. Its electronics, fine-chemicals and car industries rely on them. A disruption of supply could paralyse the Japanese economy as much as an oil embargo or food blockade. And because Japan dominates some of the technological processes that use rare earths-such as polishing hard-drive platters with cerium oxide-interrupted access would be felt worldwide. This very clear threat has forced a response.

The big trading houses such as Sojitz, Sumitomo and Mitsubishi are securing alternative supplies, supported by state financing. Companies such as Toyota, Hitachi, Nidec and TDK are working to reduce or eliminate the rare-earth elements needed in devices. Recycling programmes are being studied. The government earmarked $1 billion from a stimulus package in November to secure supplies, including funding university research and projects such as robotic deep-sea mining.

A national stockpile of the kind that already exists for rice, cereals and petrol has been mooted. There is even talk of creating a generously funded agency to acquire stakes in non-Chinese producers, possibly using the country's vast foreign-exchange reserves (at $1 trillion, the world's largest after China's). Japan's prime minister has met his Vietnamese and Mongolian counterparts to discuss new production.

Japan has been suddenly spurred to action before. The environmental crisis in the 1960s, the oil shocks of the 1970s and the strong yen in the 1980s rallied bureaucrats, politicians, business leaders, the media and the public. High energy prices forced Japan to become one of the world's most energy-efficient countries.

Japan will remain dependent on Chinese rare earths for some time. The country's resource mandarins say they have no specific target for reducing this dependency, though they reaffirm an earlier goal that Japan should control 50% of its mineral needs, including rare earths, by 2030. But the shock seems to have reinvigorated the trade ministry. Older bureaucrats are misty-eyed for the glory days when Japan was the economic power to fear.

Index | Business

BP in Russia

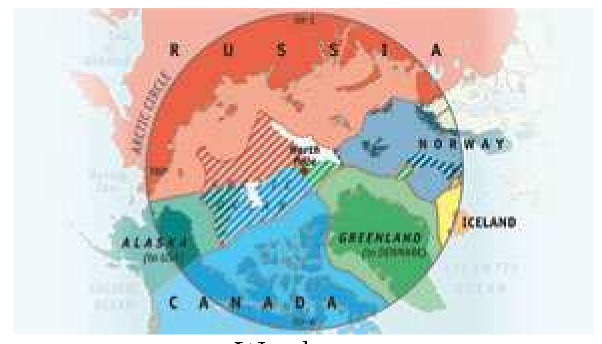
Dancing with Mr Putin

Jan 20th 2011 | *MOSCOW* | from PRINT EDITION

BP's Russian venture offers big rewards and big risks

EARLIER this month Bob Dudley was ferried along the ten-lane avenue that links Vladimir Putin's home to the Kremlin. The Russian prime minister shook hands with the boss of BP, sealing a $16 billion deal. The British oil firm will gain access to Russia's vast and deeply frozen Arctic oilfields. It will also get a 9.5% stake in Rosneft, Russia's state-controlled oil giant, to add to the 1.3% it already owns. In return Rosneft will get 5% of BP. The deal was announced to the world on January 14th.

It is the first share swap between a national oil company and a private oil major. It is also the first joint venture to explore in an area that could hold as much oil and gas as the North Sea. Far from keeping a low profile after its disastrous oil spill in the Gulf of Mexico last year, BP seems eager to prove that it is as bold as ever.



Watch our

The deal clearly makes sense for the Kremlin. Rosneft lacks the skills or capital to manage such a vast project. BP brings both, plus experience of drilling in similar terrain on Alaska's North Slope. But does the deal make sense for BP?

On the face of it, yes. Russia has some of the world's great untapped reserves of hydrocarbons. Granted, the operational risks are not trivial. Although the oil is in shallow waters, the sea ices over for eight or nine months a year. The oil may

take longer than expected to flow, and there may be less of it than BP believes. Yet these risks are outweighed by the potential rewards.

The bigger risks are political. Rosneft is no ordinary company. Its main assets were grabbed from Yukos, an oil firm the Kremlin dismantled eight years ago after its boss, Mikhail Khodorkovsky, grew too big for his boots. Yukos's main production unit was sold to Baikal Finance Group, a mysterious firm set up two weeks earlier and registered at the address of a vodka bar in Tver, a provincial town north of Moscow. A few days later it was acquired by Rosneft, which paid the bill for buying Yukos's assets. Mr Khodorkovsky is now in jail.

BP is betting that nothing so unfortunate will happen to its new deal. The British firm has plenty of Russian experience, as has its American boss. Indeed, Mr Dudley was once in charge of TNK-BP, a Russian joint venture set up in 2003, and had to flee from Moscow in 2008 after a row with BP's Russian partners. That row has now been smoothed over and BP has made pots of money from TNK-BP.

The new deal is a mutual vote of confidence, says Lucy Haskins of Barclays Capital, an investment bank. Because the Russian government now has an ownership stake in BP, and because the deal is a showcase for Russia's investment climate, Mr Putin will want it to succeed.

Yet critics, including an American congressman, find much to complain about. Oil firms often have to do business with iffy regimes, but by taking a share in Rosneft, BP is in effect buying stolen goods. Yukos's former shareholders are suing the Russian government in international courts for roughly $100 billion. One court in Sweden recently found that the Kremlin's expropriation of the company was "unlawful, not in the public interest, discriminatory and without payment of compensation". BP will surely become embroiled in this legal mess, and its reputation may suffer.

The deal with BP legitimises the Kremlin's carve-up of Yukos, and converts a portion of its ill-gotten gains into something liquid and secure-BP shares. It vindicates Mr Putin's conviction that the rest of the world operates in much the same way as Russia and that Western lectures about ethics are hypocritical. It silences Russian liberals who argued that the destruction of Yukos would deter foreign investment. And it tells foreign investors that they have no choice but to cuddle the Kremlin. That could have long-term consequences.

For BP, the potential rewards are huge but distant. After seismic testing and surveys the first test well will probably be sunk in around 2015. Full commercial production is unlikely before the early 2020s, but should continue for 20-30 years. Profits are thus years away, and much could change in Russian politics during that time.

Meanwhile, it might pay for BP to re-read Rosneft's prospectus, issued when it listed in London in 2006: "The Russian government, whose interests may not coincide with those of other shareholders, controls Rosneft and may cause Rosneft to engage in business practices that do not maximise shareholder value."

Index | Business

Food prices

The consequences of costly nosh

Jan 20th 2011 | from PRINT EDITION

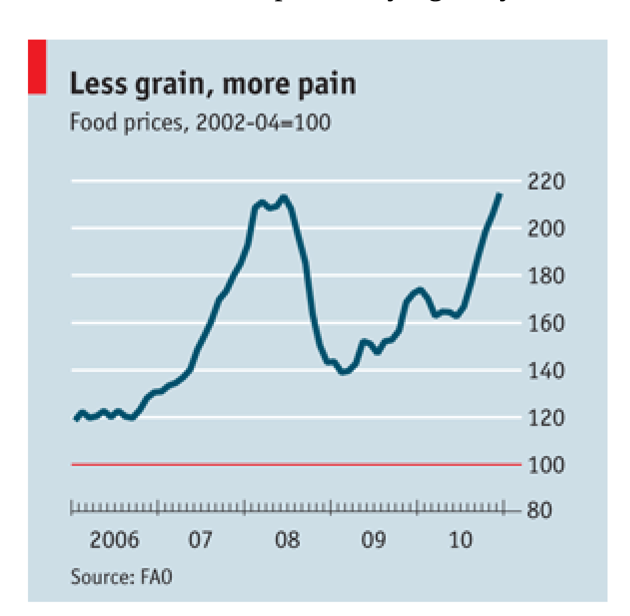
What record food prices mean for business



Spoilt child consumes rare luxury

HIGH prices are good for farmers. Low prices are good for consumers. "And we are in the middle," says Alberto Weisser, the boss of Bunge, a trader of agricultural commodities. After poor harvests in Russia, Canada and Ukraine last year, a recent heatwave in Argentina and floods in Australia that wiped out much of the country's wheat crop, everyone is grappling with pricey food.

According to the UN's Food and Agriculture Organisation (FAO), food prices last month surpassed their previous high in 2008. "The situation is not rosy, but there is no reason for panic-buying," says Abdolreza Abbassian at the FAO.



Russian, Canadian and Ukrainian farmers had a tough year in 2010, but other farmers are chortling. High prices put cash in their pockets and give them an incentive to plant more crops. As barley production in Russia slumped, the production of sorghum in Sierra Leone and Ghana surged. International brewers such as Heineken have started to experiment with sorghum beer, a cheaper brew that is strangely popular in Africa and China.

High food prices fatten traders, too. America's Cargill, the world's biggest trader of raw foodstuffs, tripled its profits in the second quarter of its fiscal year. On January 19th the privately owned firm announced that it will sell its stake in Mosaic, a fertiliser business, in a deal worth $24 billion. This will allow Cargill to stay private, after family shareholders eager to cash out had put pressure on it to float.

For makers of processed nosh, costly raw materials are a problem. ConAgra, General Mills, Kellogg's and Kraft recently raised prices for many of their wares. In December ConAgra, which makes Slim Jim meat snacks, among other delicacies, reported a 16% decline in second-quarter profits. Like other food makers, ConAgra is experimenting with smaller packages sold at the same price.

Switzerland's Nestle, the world's biggest food firm, is not yet worried. "We welcome higher prices, because they are an added incentive for farmers to produce what we need," says Robin Tickle, a Nestle spokesman. The cost of milk, cocoa, coffee and sugar, Nestle's main ingredients, account for only 12% of sales. The company protects itself against short-term volatility by using forward contracts and by buying directly from farmers with whom the firm has a long-term relationship.

For retailers food inflation is "moderately good", says Christopher Hogbin at Bernstein Research. Their share price tends to rise as investors expect higher margins. Commodity-price rises are usually passed on to consumers only after a six-month lag, thanks to forward-buying by food-makers. Food prices will rise by 6.6% this year in Britain, Bernstein forecasts, having risen by 3.1% last year.

Grocery shoppers will react by buying more discounted items and more private-label products, which are 30-50% cheaper than branded goods. They will also buy cheap chicken rather than dear beef, potatoes rather than *mangetout* and plain milk rather than fancy yogurt concoctions.

Private-label makers will sell more, but since raw materials are a higher proportion of their total costs (they don't advertise as much as posh brands), they will suffer. Most will lose more than they gain from food-price inflation. If it continues, they will have to raise their prices too. But Mr Weisser is optimistic that supply bottlenecks will soon ease. "Next year prices will come down," he says. "Farmers have so many incentives to plant more."

Index | Business

Face value: John Quelch

Teaching case studies in China

Jan 20th 2011 | from PRINT EDITION

The Western dean of a business school in Shanghai


Bettmann/CORBIS

AS HE left Rupert Murdoch's office at the *Sun* newspaper clutching a fat cheque, John Quelch realised he was interested in business. He was a history student at Oxford and had not previously given the subject much thought. But in 1972 he stepped in to help *Cherwell*, the student rag, after cocky editors (for such people can occasionally be found at that university) had driven it, in his view, into the river after which it was named.

The young Mr Quelch displayed a certain chutzpah, too. He turned up at Mr Murdoch's office with a rudimentary business plan "which wouldn't have passed muster with any accountant", and walked out with a sizeable sum. *Cherwell*'s editors

were duly dispatched. One, Peter Stothard, went on to edit the *Times*. The other, Howard Davies, became chairman of Britain's Financial Services Authority. Mr Quelch took over at *Cherwell*.



Imparting soft skills to Chinese capitalists

It was this first brush with business that encouraged Mr Quelch to take an MBA. But in the glum 1970s in Britain it was unfashionable for a student to show an interest in management. (Indeed, it would be another 24 years before Oxford opened a business school.) So he headed to America, first to Wharton and then to Harvard Business School, where he stayed for most of his career and became a star professor of marketing. He also had a brief stint as dean of the London Business School.

Now he is off to China. At the end of this month he will become the dean of the China Europe International Business School (CEIBS) in Shanghai, perhaps the best business school in mainland China.

It says a lot about business education in China that CEIBS can attract a dean of Mr Quelch's calibre. Nonetheless, he should not expect the cosy autonomy he enjoyed at Harvard. All education is tightly regulated in China. CEIBS, which opened in 1994 with help from the European Commission, is more free-thinking than most. But still, it is required to have a state partner, Shanghai Jiao Tong University. And Mr Quelch will have a shadow who bows to Beijing, in the form of a Chinese co-dean.

Business education in China is still in its infancy, but the market is growing quickly. Demand is ravenous. Haiyong Ma of the Changchun University of Science and Technology says there are more than 30,000 MBA students enrolled in 184 approved programmes. Quality is patchy, however. Fewer than half a dozen programmes are up to international standards. Many students still prefer to go overseas if they can, believing that an MBA from America, Hong Kong or Singapore carries more cachet.

CEIBS is one of the few Chinese schools that seeks to compete with the global elite. It attracts a fair number of foreign faculty and students onto its MBA programme. Unlike some other Chinese business schools, it prepares students for careers at multinational firms, not just state-owned enterprises.

It is a cliche that America is run by lawyers and China by engineers, observes Mr Quelch. This mindset is evident in business education, too, he reckons. A disproportionate number of Chinese academics research quantitative subjects such as finance and economics, he says, and Chinese students are also more likely to major in these areas.

So Chinese schools still rely on Western staff, such as Mr Quelch, for the fuzzier subjects such as human resources, marketing and leadership. These professors like to use the case-study method, but some of their Chinese students feel uncomfortable with the heated classroom debates that this requires. CEIBS embraces case studies, which will no doubt please Mr Quelch, as he is a prolific author of such studies and has so far sold 3.4m copies of them.

Outside the classroom, Chinese businesses have been slow to adopt "soft" management skills. The result, claims Mr Quelch, is a dearth of managers who can operate internationally. As Chinese firms expand around the world the demand for such people will surely grow.

CEIBS graduated 740 students from its "executive" MBA last year, a part-time course, making it the largest such programme in the world, says Mr Quelch. But there is plenty of room to expand. Mr Quelch hopes to import the American tradition of alumni donating money to their old schools. That could be ticklish. Chinese donors may expect something in return, such as a place for a thick son. (Some American donors expect this, too.) Mr Quelch lives in interesting times.

Index | Business

Live music

Pricing the piper

Jan 20th 2011 | from PRINT EDITION

An economics lesson for the concert business



Ticket touts are Bruce Springsteen's biggest fans

ARE you longing to see Take That, a British boy band approaching middle age? More than 1.3m people are. So heavy is demand for the tour, which begins in Sunderland in May, that Britain's phone network at one point creaked under three to four times the normal weight of calls. But even sold-out concerts are never really so. Plenty of Take That tickets are for sale online-at up to five times the original prices.

For the hottest acts, the concert business is good. Lady Gaga and Justin Bieber have little problem selling tickets. Yet trouble lurks below the stratosphere. Pollstar, a research firm, estimates that the 50 biggest worldwide tours grossed $2.93 billion last year-12% less than in 2009. StubHub, a large website on which tickets are traded, says the average concert-ticket price dropped by 18% between 2008 and 2010.

The long boom in live music, which saw American revenues rise from less than $1 billion in 1995 to $4.6 billion in 2009, has paused. Bands have pushed average ticket prices about as high as they can go, and tested the limits of punters' appetites with long tours. Michael Rapino, head of Live Nation Entertainment, said last year that 40% of seats routinely went unsold. To keep growing, the business will have to stop leaving money on the table.

Live music is one of the few businesses in which second-hand goods often sell for more than new ones. "As soon as a show sells out, front-row seats appear on the web for pound600," says Rob Hallett of AEG Live. Tickets to see musicians such as Bruce Springsteen, who insists that entry to his shows be cheap enough for working stiffs to afford, are particularly susceptible to what fans call "price gouging" and an economist would call price discovery. Outfits such as Ticketmaster have tried to capture some of this huge secondary market by setting up ticket exchanges. But this leaves fans confused and suspicious. It is not easy for a firm to play both the primary and the secondary market.

Change is afoot. Front-row seats for desirable shows are increasingly marketed as "premium" or "platinum" tickets, sold at a high fixed price or even at prices that float according to demand. As *The Economist* went to press, for example, you could pay Ticketmaster about pound200 for good seats at a Katy Perry concert in Manchester (the tickets' face value is pound22.50). Punters are keen: Mr Hallett says premium seats frequently sell out first.

Some live-music events have also introduced a crude version of airline-style pricing, in which tickets become more expensive over time. T in the Park, a large pop shindig held in Scotland, pioneered the practice of offering discounted "early bird" tickets to build buzz. Other pop festivals are following, sometimes with "super early bird" tickets at lower prices.

This could be pushed a good deal further. American sports teams such as the San Francisco Giants are moving to allow the prices of all individual tickets to float according to demand (which means that unpopular games become cheaper). Barry Kahn of Qcue, a software firm that creates the algorithms, says the potential for dynamic pricing is much greater in pop music because there are no season-ticket holders.

There is a hitch, however. At least four players are involved in putting on a live-music show: an artist, a promoter, a ticket-seller and a venue. Locked in perpetual squabbles over the spoils, they find it hard to adopt more sensible pricing techniques. Even the creation, a year ago, of Live Nation Entertainment, a vertically integrated entertainment giant, has not significantly changed pricing practices. Many artists say they want to shut out the touts-an impossible task.

The music business has a long history of failing to innovate. Its inability to cope with file-sharing led to the collapse of recorded-music sales and the growing dependence on live music. That part of the business now needs to improve. Time to wake up and smell the spilled beer.

Index | Business

Apple

The boss is unwell

Jan 20th 2011 | *SAN FRANCISCO* | from PRINT EDITION

Can a Jobsless Apple flourish?

ON JANUARY 18th Apple unveiled record quarterly results, with revenues rising to a whopping $27 billion and profits to $6 billion-up by 71% and 78% since the same quarter in its previous fiscal year. The bad news surfaced the day before. Steve Jobs, the firm's iconic boss, is to quit the daily grind, at least for a while, to focus on his health.

Apple has been here before. In 2004 Mr Jobs took time out after being diagnosed with pancreatic cancer. In 2009 he took six months off and had a liver transplant. On both occasions, Mr Jobs recovered and Apple didn't crumble. The firm is now America's second-largest (after Exxon Mobil) by market capitalisation.

Apple should continue to prosper this time, too. Its products are wildly popular. IDC, a research firm, predicts that the market for tablets, which Apple dominates, will more than quadruple in the next two years. The company has new versions of the iPad and iPhone in the works, which will give it plenty to talk about later this year. And Tim Cook, who will run the firm in Mr Jobs's absence, has done it before, with distinction.

Nonetheless, Apple faces pressure to reveal more about its succession plan, and about Mr Jobs's health. Candour about the succession would be unwise: those who are not picked might quit. Health is a trickier call. Even bosses deserve some privacy. But Charles Elson, a corporate-governance expert at the University of Delaware, argues that Mr Jobs's role at Apple is so crucial that it lends weight to claims that more information should be made public about his health.

Schumpeter

Nipping at their heels

Jan 20th 2011 | from PRINT EDITION

Firms from the developing world are rapidly catching up with their old-world competitors



IT IS remarkable how soon the idea that firms from emerging economies pose a serious threat to multinationals from the rich world has become old hat. "The novelty has become the norm," concludes the latest annual report on these "new challengers" by the Boston Consulting Group (BCG). But familiarity does not make that threat any less real.

Five years ago, when BCG first reported on the rising stars of the developing world, the rich world was still reeling from the shock of the purchase of IBM's personal-computing business by Lenovo, a Chinese company. That this acquisition proved something of a dud may comfort those in the old guard who suspect that the ambitions of these newcomers to enter the global stage exceed their ability to perform. Yet it has not diminished those ambitions. After a brief fall following the financial crisis of 2008, the number and size of cross-border acquisitions by the challengers rebounded strongly in 2010. In the past decade 60% of the foreign purchases by these developing-country multinationals have been of companies in the rich world; in the past two years the proportion was 70%.

In part, this may reflect the fact that the emerging economies recovered more quickly after the financial crisis, allowing their corporate champions to return more quickly to the acquisition trail. BCG has analysed 100 leading firms from emerging economies. The BRICs dominate: BCG looks at 13 companies from Brazil, six from Russia, 20 from India (six of which are part of the Tata empire) and 33 from China, with the rest spread widely. The list includes the world's largest baker (Grupo Bimbo of Mexico), meat producer (JBS of Brazil) and aluminium manufacturer (United Company RUSAL of Russia), as well as the second- and fifth-biggest telecoms-equipment firms (Huawei Technologies and ZTE, both from China).

These 100 companies are looking lively. In the past decade they have seen their revenues grow by 18% a year on average, three times faster than non-financial firms in the S&P 500. And they have managed to expand fast without sacrificing profit margins, which at 18% were six percentage points higher than those of their (non-financial) peers in the S&P 500.

BCG argues that this is because they have managed to resolve three trade-offs that are usually associated with corporate growth: of volume against margin; rapid expansion against low leverage (debt); and growth against dividends. On average the challengers have increased their sales three times faster than their established global peers since 2005. Yet they have also reduced their debt-to-equity ratio by three percentage points and achieved a higher ratio of dividends to share price in every year but one. This is despite two significant exceptions: in pharmaceuticals, where the challengers have tended to make low-margin generic drugs; and in consumer goods, where they have focused on low-cost products, leaving the higher-margin niches to established global brands.

All this is impressive, but it seems implausible that these trade-offs have been "resolved". More likely, they have been temporarily suspended during a period of unusually rapid growth. Indeed, having sprinted to catch up, the challengers may be about to discover that the real race has only just begun.

BCG identifies five trends that will determine how the tiger cubs fare against the old tortoises in the next few years. While China continues to spend heavily on infrastructure, its low-cost construction and heavy-equipment companies will surely prosper. They are not only building roads and bridges in China; one firm has won a contract to build a casino in America and more will doubtless follow. Likewise, with demand for scarce resources soaring, the miners and other commodity-based firms that have grown huge during the past few years-including several from Russia-may soon be positively elephantine.

The other three trends ought to worry the challengers a little. So far, a handful of emerging-market firms have defied the conventional wisdom that conglomerates are inherently inefficient. But will they continue to do so? As more and more of a conglomerate's activities take place far from head office, inefficiencies will surely creep in. Still, old multinationals such as America's GE insist that new technology and management techniques allow them to run sprawling operations efficiently. The challengers can surely use the same tools.

Tigers struggle to build brands

Building global consumer brands may prove tricky. So far, the tiger cubs have had more luck acquiring established brands (just as Lenovo bought IBM's PCs, Grupo Bimbo bought Sara Lee's North American bakery business) than persuading rich-country consumers to fill their baskets with the local favourites of Chinese or Egyptian shoppers. Whether such acquisitions make sense depends on the price.

Perhaps the most interesting trend is the challengers' growing reliance on partnerships. More and more, they are hooking up not with established multinationals but with other emerging-market firms, to share knowledge, penetrate new markets and spread the risk of especially hair-curling investments. And when the challengers do join forces with well-known multinationals, they increasingly do so from a position of strength.

Yet for all that, many established multinationals believe they can hold their own. Several are learning from the emerging-market challengers how to be innovative and frugal at the same time. They may not be hiring at home, but many are expanding rapidly in the developing world. For instance, according to the *Times of India*, IBM is now the country's second-largest private-sector employer. So don't write off the old guard yet.

Economist.com/blogs/schumpeter

Index | Briefing

Canada's tar sands

Muck and brass

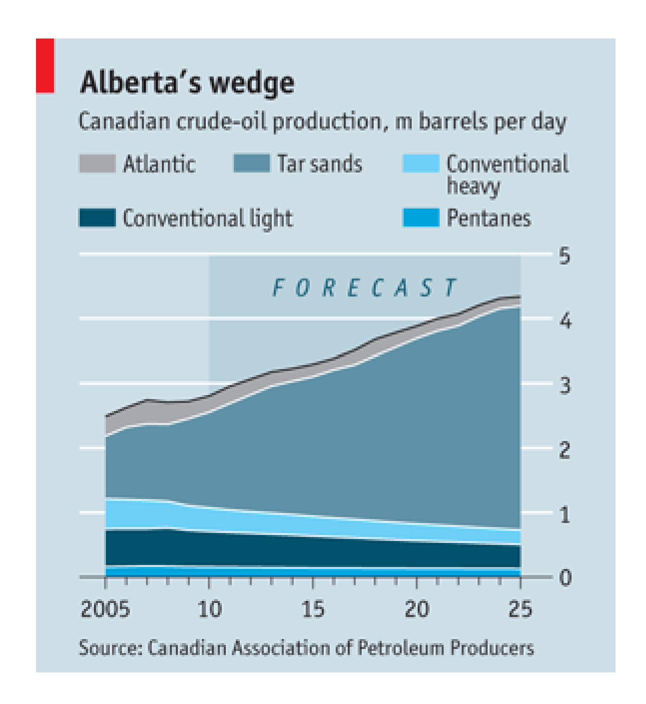
Jan 20th 2011 | *CALGARY AND OTTAWA* | from PRINT EDITION

Rising oil prices and falling production costs favour the extraction of oil from Alberta's tar sands. But environmental objections are fierce



SMOKESTACKS dot the horizon; a whiff of oil hangs in the air; gargantuan vehicles clog the highway. There is a din of heavy machinery, punctuated by blasts from cannons scaring birds away from toxic lakes. But golf courses and suburban housing make the place liveable, and some locals have grown attached to Alberta's tar sands and Fort McMurray, the town at the centre of them. "I'd like my son and grandson to work here," says a worker at one of Shell's mines.

He may get his wish. After a brief hiatus during the economic downturn, world oil consumption is rising again, pushing the price of a barrel towards $100. By 2035, believes the International Energy Agency (IEA), demand may reach 110m barrels per day (b/d), about 20% more than in 2009. For those who exploit the tar sands, which contain the world's second-largest trove of oil, this is a welcome forecast.



Despite rapid development in the past decade, the sands produce only 1.5m b/d, less than 2% of global supply. However, the Canadian Association of Petroleum Producers (CAPP), an industry group, expects output to be nearly 3.5m b/d by 2025 (see chart). Thirst for fuel is not the only thing in the oilmen's favour. The cost of production has fallen: a few years ago most firms thought the break-even price was $75 per barrel, but now companies such as Shell say new developments are economical at $50. The provincial and federal governments are unsurprisingly supportive.

There are obstacles too, mainly because of the sheer dirtiness of the business. In America, the main market, objections to the import of more of Alberta's bituminous oil are loud. And domestic opposition to exploiting the tar sands and building pipelines, which has long been fierce, is gathering momentum.

First, the economics. The IEA believes that global production of conventional oil, the stuff that can be recovered easily using drills and wells, is near or already at its peak, and that only a leap in output from unconventional sources will prevent new leaps in price. Even if countries around the world agree on measures to control carbon-dioxide emissions, says the agency, bituminous crudes like Canada's must fill a coming supply gap. That the sands lie in Canada is a rare geological fluke in the West's favour. With 70%-plus of the world's remaining oil in the hands of OPEC, half of its "free oil" is in the tar sands, notes Peter Tertzakian, chief economist of Arc Financial, an investment firm.

No self-respecting oil major has let a position in the tar sands pass by. A flock of national oil companies has joined them, led since 2005 by China's state-controlled firms. In December Total, a French oil firm, and Suncor Energy, one of the original tar-sands developers, announced plans to spend about C$20 billion (about $20 billion) on new projects in the next decade. This year alone developers will spend C$15 billion, predicts CAPP.

All this is making Alberta the flag-bearer of a new oil age, and the province is already becoming wealthy. At 173 billion recoverable barrels, the tar sands are worth $15.7 trillion at today's price. As the resource owner, Alberta captures much of this wealth, but a good deal filters through to the rest of Canada in contracts for goods and services as well as in federal equalisation payments that send some of the rich west's billions to poorer eastern provinces.

Alberta has become something of a petro-state: the oil-and-gas sector accounts for 31% of its GDP. The provincial government, run by the Progressive Conservatives for more than four decades, is naturally keen on such a generator of money and jobs. The only serious opposition, the Wildrose Alliance, is further to the right and also supports the tar sands.

Although natural resources are under provincial jurisdiction, the tar sands are a national issue too, not least because of the federal government's repeated failure to produce a plan to tackle climate change. Critics of Stephen Harper, the Conservative leader of a minority administration, say this lack of progress has everything to do with the prime minister's desire to protect the oil business and to avoid offending voters in Alberta, where his party has its core support. The environment minister, Peter Kent, upset some Canadians recently when he defended Alberta's "ethical oil", the proceeds of which would not be spent on palaces or civil wars, as they might have been elsewhere. Michael Ignatieff, the leader of the Liberals, the main opposition at federal level, also supports development of the tar sands, though he says it has to become more sustainable.

A bitumen bottleneck

However, if Canada's oilmen are to fulfil their rosy output forecasts, they will need new ways of reaching customers. America is an obvious place: Canada is already America's biggest supplier of oil and petroleum, and as the sands are exploited further its market share should only rise. By 2030, according to IHS CERA, a firm of consultants, the tar sands should supply more than one-third of America's imported oil.

But Alberta's bituminous crude needs specialised coking facilities, and its only significant outlets are refineries in the American Midwest. By 2014, says Jackie Forrest of IHS CERA, new production from the tar sands will have filled the available coking capacity. That will create a bottleneck and hinder upstream spending.



With this in mind, TransCanada, a Calgary firm, has proposed building a $7 billion pipeline, Keystone XL, to send 510,000 b/d of Albertan oil to refineries in Texas (see map). It already has a line of similar capacity, Keystone. The company says that the new one would pump $20 billion into the American economy and hand $5 billion in taxes to states on the route. Keystone XL would not only take more Canadian oil to America; via terminals on the Gulf of Mexico it could connect the tar sands with international markets as well. There are also plans to ship oil to Asia from Canada's Pacific coast.

However, these plans require political approval, and this is an awkward time for North American politicians to be weighing oily matters. You might imagine that last year's spill in the gulf would have done Alberta's onshore reserves in the sands, 40 times the size of those in the gulf, a favour. But the spill has stained the whole industry's reputation in America and has intensified long-running opposition to the sands in Canada.

Hillary Clinton, America's secretary of state, who must approve Keystone XL (because it crosses the border), has said she is "inclined" to do so; and 39 Republican members of Congress have written a letter asking her to support it. But the pipeline is meeting opposition. The governor of Nebraska, one of the states along the route, and one of its senators, both Republicans, have expressed concern. In December a union of Nebraskan farmers, not known for radical greenery, voted to oppose the project. Online petitions have drawn thousands of virtual signatures in Texas and elsewhere. And last year the Environmental Protection Agency demanded that the State Department review its assessment of the pipeline's environmental impact. This has left the decision hanging and may yet upset TransCanada's plans.

Northern Gateway, an ambitious Pacific coast proposal, would allow exports to Asia and help Canada become the "new energy superpower" Mr Harper predicted in 2006. But last month the project, which would cost C$5.5 billion and carry 525,000 b/d of oil, ran into opposition too. Leaders of First Nations in British Columbia said they would prevent the pipeline from crossing their territories. The chiefs talked of "inevitable" spills, a threat to salmon runs and devastation of their way of life. Spills last summer from pipelines in the Midwest owned by Enbridge, the company behind Northern Gateway, were scarcely a public-relations triumph.

To many critics the broader environmental legacy of the tar sands is reason enough to halt the whole endeavour. To get at the bitumen, the companies bulldoze wetlands to create vast open-pit mines. Inside them, the world's largest dumptrucks ferry paydirt to nearby separation plants, where the tarry soil is crushed and diluted until bitumen can be skimmed off. This needs lots of water and energy, and yields the notorious "tailings", a residue of sand, unclaimed bitumen, water, clay particles and contaminants. Some lakes of this have been festering for decades.

Mining accounts for just over half of production. It will become less common as shallower reserves are exhausted. Extracting the deeper stuff is less ugly but also damaging. Typically it involves drilling wells to pump steam into the ground to melt the bitumen and make it easier to suck up to the surface. Heating the steam burns much natural gas, emitting CO_2. Both methods, say the tar sands' critics, threaten local rivers, poison fish, destroy the landscape, kill wildlife and pollute the air.

The movement to stop this "dirty oil" has gathered momentum. Several American states, led by California, have passed laws designed to stop Albertan oil reaching their citizens. Some American retailers have forsworn fuel from the tar sands. A coalition of green groups has launched a campaign, "Rethink Alberta", to dissuade tourists from visiting the province until expansion of the tar sands stops.

The provincial government has begun to fight back with advertisements in newspapers and in Times Square. The industry has run ads featuring ordinary workers talking up the wonders of the oil sands. Both often offer journalists and activists tours, hoping to persuade them that things are better than they think. This candour is usually rewarded with more negative publicity. Aided by, among other things, the death of 1,600 ducks in a tailings pond and photos making northern Alberta look like a moonscape, environmentalists have succeeded in tarnishing the province's brand. "The oil sands have become the harp seal of the environmental movement," says Preston McEachern, a water scientist with the provincial government: the easiest, and softest, beast to club.

David Schindler, an ecologist at the University of Alberta, has long been publishing peer-reviewed studies showing that airborne emissions from smokestacks on upgraders, which convert the bitumen into synthetic crude oil, have polluted the Athabasca, the giant river that flows through the tar sands. His findings gained more publicity in September, when he offered photographers deformed turbot and other species pulled from the river. The images prompted a federal investigation. "I'm surprised it wasn't mounted on a block of bitumen," said an oil executive of Dr Schindler's piscine trophy.

Such weary sentiment is widespread in the industry. Sometimes it is justified. Agriculture has severely depleted south-eastern Alberta's rivers, for example, yet is allowed to use more than six times as much water as the tar sands in a region soaked with lakes and rivers. David Keith, a scientist at the University of Calgary, says the tar sands' water use is so benign, in pollution and consumption, that environmentalists ought to drop the issue. In December a report by the Royal Society of Canada (RSC) dismissed other complaints. Claims that the tar sands were the "most environmentally destructive project on Earth" were "not accurate", it said. Although reclamation of the land, a legal obligation, has not kept up with the disturbance of the tar sands, it was "achievable". The RSC added that "no credible evidence" supported worries about elevated human cancer rates downstream of the developments.

Progress by developers in cleaning up after themselves tends to win only grudging approval. In September Suncor reclaimed Pond 1, a toxic lake of residue that had been an open wound for decades. This was a small step, to be sure. The Pembina Institute, a local environmental think-tank, claims that a lot of the mature, fine tailings were merely transferred to other, larger lakes; Suncor says not. Such toxic lakes still cover 170 square kilometres (66 square miles) and will keep growing, according to the RSC. Some of them leach their waste into the ground, says Pembina, although how much is uncertain.

Suncor is promising to spend another C$1.2 billion to deal with its tailings. Rick George, its chief executive, believes that as companies share new technology, like that used by Suncor on Pond 1, the tar sands will within a decade look like any other mining operation, with only one lake open, temporarily, per mine. Only since the turn of the century have the companies cracked the economics of the tar sands, argues Mr George. Now they can concentrate on greening them.

Whether Alberta's government can be relied on to promote greener tar sands, however, is questionable. The province has been a model of laissez-faire. In private many oil-industry executives wish it would be more diligent as a regulator, feeling that its lax approach has become a threat to developments, not an incentive. Most of the province's best minds don't join the government in Edmonton, goes a frequent lament, but head for deep-pocketed oil companies in Calgary.

Both the RSC's report and another commissioned by the federal government, also released last month, demolished Alberta's claims to have monitored the tar sands' impact adequately. Regulators had "not kept pace with rapid growth" and the province's environmental assessments had "serious deficiencies" leaving them below "international best practice", the RSC said. The federal report rubbished the province's water-monitoring, which involved handing the job to an industry body-putting the "fox in charge of the henhouse", says Dr Schindler. After December's reports both the federal and provincial governments promised new measures to improve monitoring, an admission that the current arrangements are inadequate. Yet Mr Kent, the federal environment minister, has flatly rejected Dr Schindler's research into the pollution of the Athabasca.

Clean and scrub

Some environmental problems could be solved fairly easily. One long-standing idea is to create a large wildlife refuge in areas that will eventually be tapped for bitumen. Only after a developer has restored land it has already mined could it begin tearing up an area of equivalent size within the refuge. Pembina says up to 40% of the region could be protected this way, with no impact on oil production. Various nasties Dr Schindler found in the Athabasca could be dealt with by adding "simple off-the-shelf" scrubbers to upgraders' smokestacks, he says. Though they are not legally required, many companies have added them to capture sulphur dioxide. Enforcement of rules to make operators deal safely with half of their tailings by 2013 has been patchy. Many operators will miss the deadline, says Pembina, and another rule is needed for the other half.



Filthy rich

Outside Canada, most complaints are about the tar sands' CO_2 emissions. Here too, confusion abounds. Some critics, calculating emissions from extraction through to refining ("well to tank"), say fuel sourced from the sands is up to three times more carbon-intensive than others consumed in America. But from "well to wheels", counting emissions from cars' exhaust pipes, tar sands are only 5-15% dirtier, says IHS CERA. Most CO_2 comes from burning the petrol, not digging up the oil.

Whatever the measure, Alberta lacks an adequate strategy to deal with emissions. Its climate-change targets would allow emissions to grow until 2020. And those from the tar sands could triple in the next decade, as more oil is extracted by steam-based methods. Still, the sands are carbon-emitting minnows. Just 5% of Canada's CO_2, about 0.1% of the world total, comes from the developments, says CAPP. If people are serious about fighting climate change, argues Dr Keith, they should worry first about coal-fired electricity, whose emissions in America dwarf those from the tar sands. Andrew Leach, of the Alberta School of Business, calculates that the tar sands create about C$500 of value-added per tonne of CO_2, against C$20-30 from coal-fired power stations.

Peter Silverstone, of the University of Alberta, argues in a recent book that the province should levy its tar-sands royalties on a scale that reflects each project's emissions. Some companies may welcome this. Shell already adds a nominal carbon levy of $40 per tonne to its projects when deciding whether to invest in the region, calling this a "licence to operate", even though Alberta's own carbon tax is just C$15 per tonne. With hefty provincial funding, Shell is also among those hoping to capture CO_2 emitted by one of its tar-sands upgraders. Alberta is investing C$2 billion in carbon capture and sequestration, its favoured way of cleaning up emissions.

Environmentalists may regard such schemes with mixed feelings. Carbon-neutral extraction would do nothing to cut the bulk of oil-related emissions that come from combustion. Eco-friendlier tar sands could also encourage unconventional development elsewhere: Jordan, Madagascar, Congo and Venezuela, where the government claims a reserve of bitumen even greater than Alberta's, may be less open to environmental scrutiny. Kill Alberta's tar sands, say some, and rising crude prices would choke oil consumption and force an era of clean energy into being.

This would be a hard argument to make, especially in the United States. Even if America's consumption keeps shrinking, it will remain the world's biggest oil buyer for decades: foreign supplies will grow more, not less, important in its market. Ezra Levant, author of a recent polemical defence of the tar sands, argues that Americans would rather buy from Canada than from Venezuela and the Middle East.

Meanwhile in Calgary, oilmen expect a pipeline to the Pacific, and in effect to Asia, to come sooner than later, especially if Keystone XL is blocked. A settlement with First Nations opposed to Northern Gateway, involving both money and environmental safeguards, could hasten that. Chinese oil companies would happily take delivery, might be less fickle customers than the southern neighbours and might help Canada fulfil Mr Harper's dream of energy superpowerdom. Many Americans, however, might ask why the State Department had allowed a rising economic rival into such a vast oil reserve.

China's currency

Stranger than fiction

Jan 20th 2011 | *HONG KONG* | from PRINT EDITION

The plot thickens on the rise of the "redback"



IN HIS new book "Super Sad True Love Story", the novelist Gary Shteyngart depicts a future in which an overstretched America depends on the forbearance of its Asian creditors. That scenario is not, sadly, a great test of the author's imagination. In this fictional world, America's currency and China's are still closely linked. But nervous Americans peg their greenbacks to the yuan (worth about $4.9), not the other way around.

America presents a "grave risk to the international system of corporate governance and exchange mechanisms," says a Chinese central banker after a trip to New York. That is from the novel. The "international currency system is the product of the past," says China's president before a trip to Washington, DC. That is from real life. In response to a question posed by the *Wall Street Journal* and the *Washington Post*, Hu Jintao echoed a complaint made by the (real) governor of China's central bank, Zhou Xiaochuan, in 2009. The financial crisis, Mr Zhon said back then, reflects the "inherent vulnerabilities and systemic risks in the existing international monetary system."

These observations are partly political, of course. America has long complained about China's cheap currency, raising the issue at multilateral forums like the IMF and the G20. China has taken to responding in kind. If America is going to gripe about the yuan's rate, then China will complain about the dollar's role.

What is that role? The dollar is more than just a reserve currency. For many countries, it is a "key" currency. Their exchange rates revolve around the dollar, just as the notes on a scale centre on a musical key. Their governments fear that if their currency falls too far against the dollar, inflation will take hold or the country's dollar debts will become too heavy to bear. If their currencies rise too far against the greenback, their exporters will lose out wherever customers pay in dollars.

But the dollar is not always perfectly pitched. Mr Zhou and President Hu worry that America is printing too much money to try to revive its own economy, regardless of the consequences abroad. To stay in tune with a falling dollar, other central banks will have to print more of their own currency, risking inflation and asset-price bubbles. "The monetary policy of the United States has a major impact on global liquidity and capital flows," Mr Hu told the *Journal* and the *Post*, "therefore, the liquidity of the dollar should be kept at a reasonable and stable level."



Mr Hu admitted that making the yuan "an international currency will be a fairly long process." Still, that process has begun. His government now seems keen to promote the yuan in international trade. In June it allowed most of the country to pay for imports in yuan and 365 Chinese companies to sell exports for the currency. Last month, it expanded the number to 67,359. By the end of November, trade worth 385 billion yuan ($58 billion) had been settled in China's currency (see chart).

About 80% of these transactions involved exports to China not imports from it. Foreigners seem keener to sell stuff for yuan, rather than buy stuff with them. As a result, a stream of yuan has flowed beyond China's borders, most of it collecting in deposits in Hong Kong. This offshore pool of "redbacks" is still small but is becoming deeper and more liquid. In Hong Kong, yuan deposits probably reached 300 billion by the end of 2010 (see chart).

Once offshore, these redbacks can frolic in Hong Kong's free markets. They can be bought, sold, borrowed, lent, swapped and hedged. A growing list of issuers, from McDonald's to the World Bank, have sold so-called "dim sum" bonds in Hong Kong in order to borrow these offshore yuan. But the mainland remains enclosed by a levee of regulatory controls. Yuan can leave the mainland in payment for an export to China; they can return in exchange for an import from China. But all other routes in and out are tightly controlled.

In August the government said that certain lucky banks could invest some of their offshore yuan in the interbank bond market on the mainland. This month it said that companies making direct investments abroad-acquiring foreign firms or building foreign factories-could pay in yuan. Likewise, it permits companies that have raised yuan offshore to invest the proceeds on the mainland, but only in their own operations or other direct investments. The process is unpredictable and can take weeks or even months, says Donna Kwok of HSBC, which is partly why so few mainland companies have borrowed offshore, despite the cheap rates on offer.

China seems happier to allow capital to flow in the opposite direction. Its banks are pushing yuan loans and trade credits, especially to customers in emerging economies. But lending in yuan is not as easy as China might wish. When India's Reliance Power ordered equipment from Shanghai Electric, three Chinese banks offered the Indian firm a loan of $1.1 billion over more than 13 years. The deal demonstrates China's manufacturing prowess and its prodigious ability to lend. But it also reveals how far the yuan has to go. Less than 0.5% of the loan was in yuan. The rise of the redback will be a super, true story. But as Mr Hu cautioned, it will also be a long one.

Index | Finance and Economics

Shorting China

Waiting for the great fall

Jan 20th 2011 | *NEW YORK* | from PRINT EDITION

Some hedge funds continue to short the China dream

A YEAR has passed since Jim Chanos, a well-known short-seller, predicted in a speech at the London School of Economics that China's property boom would end up like "Dubai times 1,000, or worse". Easy credit and frenzied investment, he argued, were creating a huge bubble in the prices of property and other assets. Bears also believed that the high degree of state direction in the Chinese economy was not an advantage, as many admirers liked to imagine, but a chronic weakness that fostered opacity, corruption and the misallocation of capital. When the pessimists dreamed of China they did not see Pudong's glittering skyline, but newly built ghost cities hidden in the hinterland and yuppies drowning in debt.

China has not plunged as Mr Chanos and a few fellow bears said it would. But he insists it has "already been a pretty good short". Last year Chinese stocks performed poorly. The Shanghai bourse fell by about 14%. Most mainstream investors and plenty of Chinese officials also now fret about China's ability to curb inflation and its state-controlled banks' capacity to lend so freely while avoiding a bad-debt problem. In sum, "2010 was a year when a lot of China bears, if they weren't totally vindicated, were given a lot of credibility," says Jim Rickards, senior managing director of Tangent Capital, a merchant bank that advises hedge funds.

If making your mind up about whether China will get into trouble is hard, the mechanics of betting against it are tricky too. "I've encountered a huge amount of interest over the last year in shorting China," says someone based in Asia who advises hedge funds on the country. But because short-selling is mostly prohibited in mainland China, it is only practical to bet against the shares of those mainland companies that are listed offshore, mainly in Hong Kong and New York.

A few bears are really betting against companies, not the wider economy. Some of the more heavily shorted Chinese stocks listed on NASDAQ, an American exchange, are considered by pessimists to have poor-quality profits and to be hard to understand. But most short-sellers have a broader horizon. One popular view is that if China's property bubble bursts it will drive down the share prices of Hong Kong-listed property firms. Three of the ten most popular stocks to short on the Hong Kong stock-exchange are property companies, according to Data Explorers, a research and analysis firm.

Shorting the world's big commodity firms is another obvious strategy. A recent report by Fitch, a ratings agency, estimates that if China's growth falls to 5% this year (from the projected 10%), global commodity prices could plunge by as much as 20%. Many big Western natural-resources firms, particularly those that dig up iron ore and other metals, have come to rely on China as by far their biggest customer. Their share prices would tumble if the country's construction and capital-expenditure boom abruptly ended. A derivative of the same trade is to short the currency of Australia, a big raw-materials supplier to China.

Other hedge funds are placing even more oblique bets. Eclectica Asset Management, a firm based in London that has launched a fund focused on China, has reportedly taken out credit-default swaps on bonds from Japanese industrial companies, which may be vulnerable to a reversal of China's construction boom.



Overall, though, it is hard to argue that investor sentiment has shifted markedly against China. True, some bulls are becoming more cautious. This week Tim Moe, chief Asia-Pacific strategist at Goldman Sachs, said the bank had "held on too long to our overweight position in China last year", and added that "the longer-term picture of Asia outperforming the US is taking a breather." But total short positions on Chinese stocks listed in America or Hong Kong have not jumped in

the past year and are at fairly low levels (see chart). "Mega-bears" are still a small minority. But as any short-seller will tell you, being lonely is just the precursor to being right.

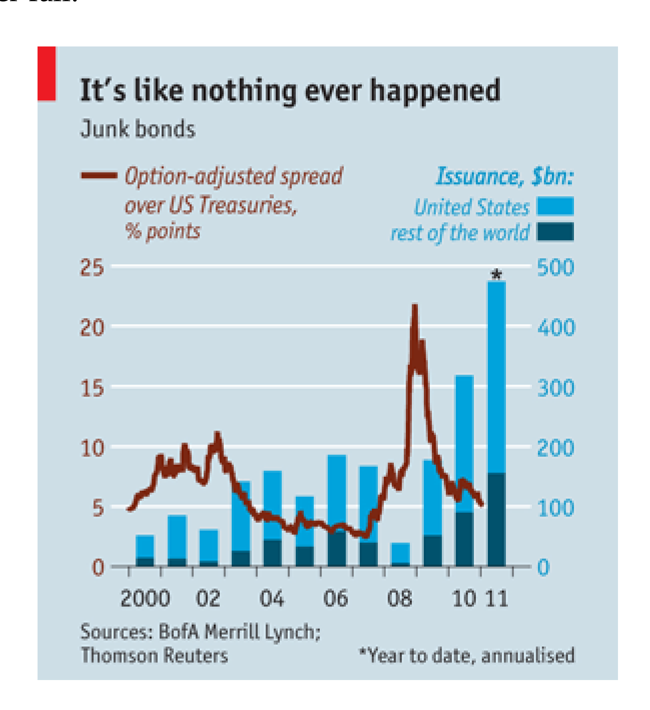
High-yield bonds

Back on the junk

Jan 20th 2011 | *NEW YORK* | from PRINT EDITION

Junk-bond prices look frothy again

IN ONE of the most eye-popping episodes of the financial crisis, high-yield bonds-those rated "junk", or below investment grade-traded at an average interest rate of more than 20 percentage points above Treasury bonds in late 2008 as investors dumped risky assets. The junk-bond market's subsequent rebound has been nearly as dramatic. So much so that some reckon it is ripe for another fall.



High-yield bonds returned a handsome 15% last year after a stunning 58% in 2009. The extra interest rate that investors demand to hold junk has fallen to its lowest since late 2007 (see chart). Borrowers have rushed to take advantage of strong demand: after record issuance in 2010 the pace has accelerated in the first two weeks of 2011. This is a bonanza for investment banks, which earned $5.8 billion in junk-bond fees last year, the most ever and $1.5 billion more than they made from investment-grade bonds, according to Dealogic.

Borrowers are keen to strengthen their balance-sheets while the going is good, by replacing costly debt with cheaper, longer-term paper. Last month Novelis, an aluminium company, borrowed $2.5 billion, allowing it to rejig a "tower of debt" due in 2014-15 over a much longer period, says Steve Fisher, the chief financial officer. Kenneth Trammell, his counterpart at Tenneco, which makes emission-control systems, calls a recent $500m issue a "no-brainer" that saved $9m in annual interest costs.

Bulls point to a sharp decline in distress. The global high-yield default rate, 13.1% in 2009, was just 3.1% by the end of 2010. Moody's expects it to fall further this year to 1.9%, the lowest in two decades. High-yield strategists predict that 2011 will be a solid year, with returns of 8-10%.

Optimists also point out that spreads over Treasuries, which investors care about more than absolute interest rates, are near their historical average and double their pre-crisis lows. Using a model that crunches default risk, credit availability and other measures, Martin Fridson, a veteran junk-watcher at BNP Paribas, deems the market pretty fairly valued. "Whatever

the future may hold, pundits who are bearish on high yield cannot justify their stance on grounds of valuation," he asserts. "Given where the fundamentals are, the spread is actually a touch more than it should be."

Perhaps, but risks lurk. Investors should worry about the loosening of bond covenants (restrictions that borrowers accept on leverage and the like) over the past year-an echo of the frothy days of 2006-07. Novelis negotiated an "extremely attractive" package that gives it more flexibility in some respects than it would have had before the crisis, says Mr Fisher.

Some strategists are telling clients to shift into equities, which tend to outperform corporate debt in economic expansions, not least because acquisitive firms bid up targets' share prices. And if the recovery stumbles, so might junk bonds. A deepening of the euro crisis could push high-yield default rates back above 6%, reckons Moody's. Jim Casey, co-head of leveraged finance at JPMorgan Chase, the leading underwriter, sees no bubble but admits that "the opportunities have diminished in recent months and the risks have grown."

Some see higher interest rates and inflation as the big threats. As rates rise, older bonds with lower coupons are worth less to their holders. This should be part of every bond-buyer's calculus. But wrenching rate rises can still wreak havoc. Junk bonds have historically been less sensitive to interest-rate swings than Treasuries or high-grade corporate debt, because their prices are more closely linked to the credit quality of individual issuers. Nevertheless, an inflation scare accompanied by a tightening of monetary policy is, as a banker puts it, the market's "potential nemesis".

Buttonwood

Worlds apart

Jan 20th 2011 | from PRINT EDITION

Two contrary views on the outlook for markets



INVESTORS could visit two very different worlds on January 17th, provided that they worked in London. In the morning Goldman Sachs held its global strategy conference in its Fleet Street offices; in the afternoon the strategy team at Societe Generale, a French bank, held a seminar in a Grosvenor Square hotel.

The presentations differed vastly in manner, as well as matter. The Goldman team was formally dressed in suits and ties; its book of graphs was bulky enough to be an aid in fending off muggers. The SocGen team appeared to have dressed either for an outward-bound course or a company disco; its slidebook could fit into a back pocket. The regulatory

disclosures accompanying just one Goldman speech were longer than the entire supporting material presented by Albert Edwards, SocGen's global strategist.

The overall messages could not be farther apart. In the Goldman world the forecast is for eternal sunshine; visitors to the SocGen world would need to carry an umbrella and a gas mask. But at least SocGen visitors could smile while they suffered; one slide focused on the resemblance between Ben Bernanke, chairman of the Federal Reserve, and Rudolf von Havenstein, president of the Reichsbank during Germany's hyperinflation.

Goldman believes that global economic growth will be stronger than expected this year, inflation will stay low and investors in American equities will earn returns of 15-20%. In America, consumer spending will grow by 3.5% as unemployment falls while businesses will improve their profit margins, even as commodity prices rise.

Goldman's view of the world seems dominated by its faith in the emerging economies, notably the BRICs (Brazil, Russia, India and China), an acronym coined by Jim O'Neill, a strategist who has been promoted to head its asset-management division. Western observers constantly underestimate this development, in Mr O'Neill's view; for example, the value of Chinese consumption has risen by $1.6 trillion over the past decade and could rise another $400 billion this year.

Equities are cheap in Goldman's model, which focuses on the risk premium over government bonds. There is no graph of the cyclically adjusted price-earnings ratio, another valuation measure, in its presentation book, although the subject did arise in questions at the conference: David Kostin, a strategist, said Wall Street was slightly above fair value on this measure. That will be a surprise to anyone who follows the website of Professor Robert Shiller at Yale (www.irrationalexuberance.com). It puts the ratio at 23, about 40% above the long-term average.

Indeed, all four speakers at the SocGen event used a chart of the cyclically adjusted ratio. In the past it has been a very useful long-term tool. Andrew Lapthorne, SocGen's quantitative strategist, points out that buying equities when valuations are at current levels has delivered average historic real returns of just 1.4% a year.

Mr Edwards and his team have long propagated their "Ice Age" thesis, in which deflationary pressures drive down the valuation of equities relative to government bonds, as occurred in Japan. At times, for example during the dotcom bubble in the late 1990s, this view has been wholly out of fashion. But if Mr Edwards can be dubbed a perma-bear, most investment-bank strategists tend to be perma-bulls.

Which group is right? There was no sign that investors were playing favourites; both meetings were packed. The mood is not yet reminiscent of 2000-style euphoria or 2008-style despair.

In Goldman's view the bears are not taking sufficient account of the growth of the developing world and are focusing too much on crises in small countries like Greece and Portugal. Fiscal and monetary stimulus will cause the world to recover, as it has many times in the past.

The SocGen case is that the outlook was fundamentally changed by the financial crisis of 2007-08. The debt-fuelled model is broken. Central banks are trying to revive it again, by keeping interest rates low so that asset prices will rise and consumer confidence is restored. But the result will just be another bubble and another bust. In the words of Mr Edwards: "Basing economic growth on loose monetary policy driving up asset prices is simply doomed to failure."

Buttonwood is inclined to side with the SocGen team. But in the short term, cheap money is a potent force. Experience suggests it can drive asset prices well above the levels that cautious investors are willing to stomach.

Index | Finance and Economics

Goldman Sachs and Facebook

A risk too far

Jan 20th 2011 | *NEW YORK* | from PRINT EDITION

Goldman's judgment may be flawed, but so are America's securities laws

TALK about bad timing. On January 4th Goldman Sachs said it would buy a stake in Facebook and help its clients to invest in the internet firm too. On January 11th it released a business-standards report aimed at reassuring clients that they came first. Now Goldman has discriminated against hundreds of them. It has reluctantly excluded American clients (and its own partners) from the private share placement for Facebook, citing "intense media coverage". Only overseas investors will be able to buy into the $1.5 billion offering.

Goldman's fear was that the hoopla surrounding the deal could have been construed as a "general solicitation" that breached America's draconian laws on placements. It is implausible that Goldman tried to drum up public interest. But details of the deal were leaked (by whom is unclear) and the press had a field day. That was enough to persuade Goldman that the risks of going ahead, and being accused of feeding the hype, outweighed the loss of face from shutting out a segment of its customer base.

The firm insists it was not arm-twisted by regulators. But they loomed large in its thinking. It would have been down to the Securities and Exchange Commission (SEC) to judge, after the placement's completion, whether it complied with the rules. If it was found wanting, either Goldman (as underwriter) would have had to buy the stock back at par, or Facebook would have had to go public. The SEC might well have taken a tough stance given that it is investigating trading in private markets and is keen to look relevant after a dire performance in the crisis.

Though most of the excluded clients are said to understand Goldman's predicament, some are angry. The firm's relationship with Facebook has also grown tense. The real villain of the piece, however, may be the 1930s laws that put such a straitjacket on those leading private placements. What does it say about securities regulation when information disseminated to an interested public by the media makes an offering potentially illegal for Americans to take part in but not the rest of the world? In this case, laws designed to protect vulnerable investors have merely ended up preventing a bunch of sophisticated ones from partaking in what might be a juicy opportunity. If the affair sparks a rethink of those rules, some good may come of it.

Index | Finance and Economics

Commodity prices and global growth

Back with a vengeance

Jan 20th 2011 | from PRINT EDITION

Rising commodity prices both reflect and threaten the world's economic recovery

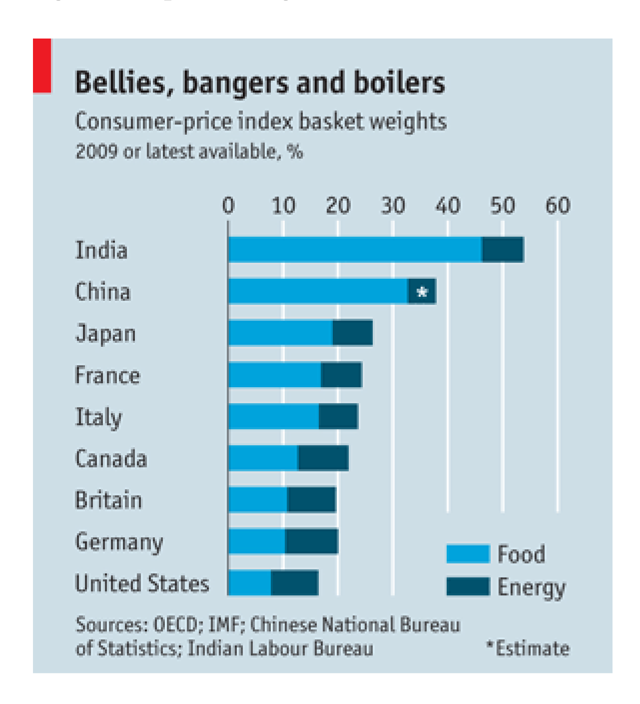
COMMODITIES are partying like it is 2008. The oil price stands at its highest since October of that year, just shy of $100 per barrel. World food prices-as measured by *The Economist*'s index-are back at their peak of July 2008. Copper prices, which have jumped by 17% since the start of November, are at an all-time high. The recent gains reflect reduced concern about global economic prospects, helped along by the Federal Reserve, which announced a second dose of quantitative easing in November last year.

The worry is that rampant commodity prices may cause another wobble in the world economy. Higher commodity prices act like a consumption tax, transferring income from households and companies which use the resources to companies and countries that produce them. As the producers tend to save more of their income than the consumers, more expensive commodities bear down on global demand.

The oil price has pushed the world into recession in the past, most obviously in the 1970s. Blame for the recent great recession is typically laid at the door of the financial crisis, but it is often forgotten that America's economy was shrinking for nearly a year before the collapse of the investment bank Lehman Brothers.

James Hamilton, an academic at the University of California, points the finger at oil. He reckons that the rise in the oil price from early 2007 largely explains the downturn between the end of 2007 and the third quarter of 2008. Households

tightened their purse-strings as they found themselves devoting almost 7% of their spending to energy. That share had fallen back to 5.5%, before the latest surge in oil prices began.



Outside America, food has a bigger share than energy in consumers' shopping baskets-and thus in inflation too (see chart). In developing countries, rising food prices can be a human as well as an economic disaster. In Asia in early 2008 a spike in the price of rice led to widespread unrest and desperate attempts by governments to secure more supplies. In December in India, for example, food prices rose at an annual rate of 14%, and there has been a run on onions, a dietary staple.

As well as taxing consumers, or worse, dearer commodities push up overall inflation, as the latest numbers from the euro area and Britain show. Although textbooks suggest central banks should "look through" a one-off increase in commodity prices, which provides only a temporary boost to inflation, monetary policymakers fret about second-round effects.

With inflation now above the European Central Bank's comfort zone and almost double the Bank of England's target, pressure to raise interest rates is growing. So far, these central banks have held back, in view of the big cuts to public spending taking place, sluggish growth and idle resources. Unlike some emerging economies, where rates have been raised, these rich economies are far from overheating. But higher commodity prices may tip the balance of risks, causing policymakers to lose their nerve. Tightening policy would act as a further drag on growth, possibly threatening the recovery.

Some comfort can be taken from the fact that, although some commodity prices are above 2008 levels, inflation rates of commodities are still below what they were then. For instance, agricultural food prices are up 37% on a year ago, whereas in 2008 the rate of increase peaked at 75%. Jonathan Anderson, an economist at UBS, a bank, reckons that global food prices would have to rise by another 50% from current levels for headline food-price inflation to reach the heights of 2008. And he thinks that is unlikely: there is no sign of the massive energy and fertiliser price increases seen in 2008. That is partly because annual oil-price inflation is running at 17%, compared with 100% at its peak in 2008.

But the balance between oil supply and demand is a concern. Whereas recent increases in many food prices reflect temporary supply disruptions (such as droughts and flooding), the rise in the oil price is due to strong demand and stagnating production. Lutz Kilian, at the University of Michigan, suggests that unless energy consumption is reduced or new supplies found a full recovery from the financial crisis will push the oil price back to its highs of mid-2008.

Furthermore, commodity prices are rising at an early stage in the economic cycle. Jeffrey Currie of Goldman Sachs worries that, as American oil demand recovers, it will "bump up against" China, which is consuming 23% more oil than it did in 2007-as well as 63% more copper, 18% more cotton and soybeans and a few more cases of wine too (see next article). With the global recovery fragile and unbalanced, higher commodity prices are the last thing the world needs right now.

Index | Finance and Economics

Commodity prices

Fluid logic

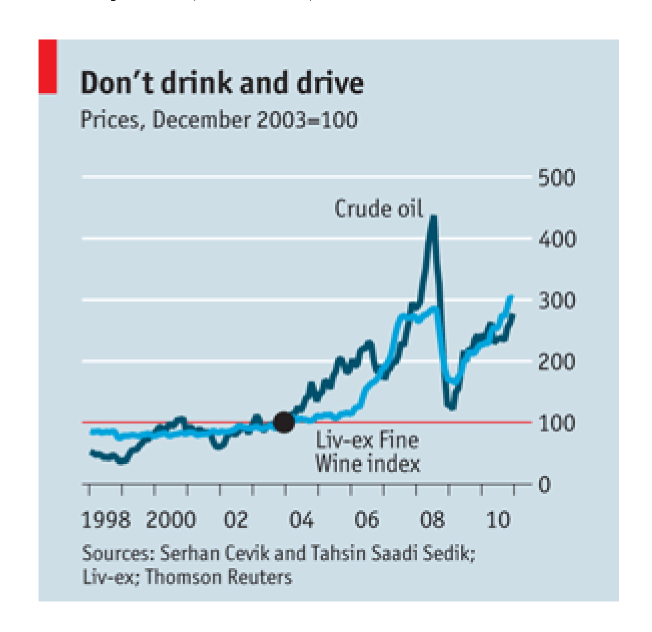
Jan 20th 2011 | from PRINT EDITION

Why two economists have found it increasingly hard to distinguish oil from wine



Some more unleaded, Sir?

A BOTTLE of Chateau Petrus '82 can cost over $5,000, whereas the equivalent volume of crude oil sells for less than 50 cents. Chateau Brent may taste a tad rough, yet fine wine and crude oil have more in common than you might think. Their prices have risen and fallen in step in recent years (see chart).



Wine experts usually explain price movements by supply-side factors such as the effects of the weather and age, but research by Serhan Cevik and Tahsin Saadi Sedik, economists at the IMF, finds that supply has only a small impact on prices. Instead, fast economic growth in emerging economies has been much more important in recent years-as is the case for oil and other commodity prices.

Between 1998 and 2010 there was a correlation of over 90% between changes in oil and wine prices. This encouraged the two economists to build an economic model to explain swings in the prices of crude oil and fine wine using the same variables: oil or wine production, growth rates in rich and emerging economies, and a measure of global excess liquidity.

Emerging economies have accounted for more than 100% of the increase in global oil demand since 2000, while oil consumption in rich countries has declined. Likewise, rising incomes in emerging economies have spurred wine drinking,

whereas consumption in Europe, notably France and Italy, has fallen. China (including Hong Kong) overtook Britain last year as the biggest export market for Bordeaux wines. So for both wine and oil, emerging economies now account for the bulk of incremental changes in demand and therefore have the biggest influence on prices.

Not only are emerging economies growing faster, but their growth is more energy intensive. Likewise, an increase in income seems to lead to a bigger rise in wine demand in these economies than in the rich world, and so gives a bigger boost to prices. A slowdown in emerging economies, on the other hand, would dent prices by much more.

In the West investing in fine wine instead of equities, bonds or commodities has become something of a faddish way to diversify one's portfolio. But if wine prices closely track traditional commodities such as oil, buying wine will not reduce overall risk. In contrast, much of the increased demand from Asia is for imbibing, not investment. Western wine snobs sniff that the Chinese do not know how to drink good wine, horrified by reports of red wine being mixed with Coca-Cola or being knocked back in one. A case, perhaps, of sour grapes.

Index | Finance and Economics

Economics focus

The beautiful and the damned

Jan 20th 2011 | from PRINT EDITION

The links between rising inequality, the Wall Street boom and the subprime fiasco



THERE was not a single year between 1952 and 1986 in which the richest 1% of American households earned more than a tenth of national income. Yet after rising steadily since the mid-1980s, reckon Thomas Piketty and Emmanuel Saez, two economists, in 2007 the income share of the richest percentile reached a staggering 18.3%. The last time America was such an unequal place was in 1929, when the equivalent figure was 18.4%. The similarities in the evolution of income inequality in the years leading up to the Depression and the global economic crisis make for one of the most striking parallels between the two episodes. Some talk of a repeat of the Roaring Twenties, when Jay Gatsby threw lavish parties at his Long Island mansion-although this time round, the dubious profits have been made from real-life finance, not fictitious bootlegging.

Economists have been thinking hard about the causes, extent and consequences of the recent rise in inequality. At the annual meeting of the American Economic Association (AEA) in Denver this month, there was a spirited debate about one of the most controversial hypotheses so far. That has been advanced by Raghuram Rajan, of the University of Chicago

Booth School of Business, in a recent book, "Fault Lines". He argues that increased inequality-more precisely, the political response to it-helped to cause the financial crisis.

Mr Rajan reckons that technological progress increased the relative demand for skilled workers. This led to a widening gap in wages between them and the rest of the workforce, because the supply of the skilled did not keep pace with demand. This reasoning is widely accepted. But Mr Rajan goes further than most when he argues that this growing gap lay behind the credit boom whose souring precipitated the financial crisis.

Governments, he argues, could not simply stand by as the poor and unskilled fell farther behind. Ideally, more should have been spent on education and training. But in the short run, credit was an easy way to prop up the living standards of those at the bottom of the economic pile. This was especially true in America, with its relatively puny welfare state.

Mr Rajan thinks, therefore, that it is no coincidence that America in the early 2000s saw a boom in lending to the poor, including those folks that banks used to sniff at. He points to the pressure the government put on the two state-backed housing giants, Fannie Mae and Freddie Mac, to lend more to poorer people. Affordable-housing targets, slacker underwriting guidelines and the creation of new "low down-payment" mortgages were all used as instruments of public policy.

The push for affordable credit worked. Subprime mortgages, whose share of all mortgages serviced rose from less than 4% at the turn of the century to a peak of around 15% before the crisis, were the most visible examples of this. They helped push American home-ownership rates to record highs. But the credit boom also inflated an enormous housing bubble, whose collapse precipitated a financial crisis brought on by defaults on those very subprime mortgages. According to Mr Rajan, therefore, well-intentioned political responses to the rise in inequality that many found disturbing ended up having devastating side effects.

This is a provocative idea. But do the facts support it? Two prominent economists-Daron Acemoglu of the Massachusetts Institute of Technology and Edward Glaeser of Harvard University-argued at the AEA meetings that Mr Rajan's hypothesis, for all its plausibility, is flawed. Neither critic doubts that inequality rose and that poorer people gained access to more credit. But they disagree with Mr Rajan on the link between the two.

Mr Acemoglu argues that the expansion in credit came far too late for Mr Rajan's hypothesis. The subprime boom began around 2000. Yet those at the bottom of the income distribution were getting hammered by technological change in the 1980s. Since then, the least-skilled workers in America have not become still worse-off, largely because they work in service industries which are hard to automate. Inequality has continued to rise because the rich have done even better; it is those in the middle who have fared relatively poorly. Why would the state try to help the poorest at a time when they were doing better than before?

Mr Glaeser has a different criticism. He thinks that the role of easy credit in the housing bubble was not as large as Mr Rajan believes. He refers to research by Atif Mian, of the University at California, Berkeley, and Amir Sufi, of the Booth School, which shows that increased mortgage availability pushed up American home prices by only around 4.3%. This was a small fraction of the rise in prices during the boom. Irrational exuberance and a willingness to bet on prices rising for ever were probably much bigger contributors to the bubble than credit expansion.

Let's all agree to blame the speculators and lobbyists

Mr Acemoglu does believe that there is a link-albeit not a causal one-between increased inequality and the crisis. He thinks both were the consequence of politicians' willingness to deregulate the financial sector, which partly reflected the industry's lobbying prowess. A consequence, documented by two more economists, Ariell Reshef and Thomas Philippon, was that salaries in finance soared, causing a substantial part of the explosion in top incomes noted by Messrs Piketty and Saez. Runaway lending and lax standards, which fuelled the boom and contributed to the crisis, were others. So he thinks Mr Rajan is right to focus on politics but that they did not play out in quite the way he believes.

Ultimately it may be hard to prove a causal connection between inequality, subprime lending and the Wall Street boom. Even so, most economists at the AEA gathering agreed that the three forces combined in the American economy in an unsustainable and unhealthy way. To misquote "The Great Gatsby", the rock of the world was founded securely on a fairy's wing.

The waiting game

Jan 20th 2011 | from PRINT EDITION

Chastity before marriage may have its uses after all


Eyevine

WHEN is it the right time to do the deed? If priests had their way, it would be shortly after the wedding ceremony-but recent studies show such advice is rarely heeded. Roughly 85% of the American population, for example, approves of premarital sex. Faced with numbers like that, what hope do the Vatican and its ilk really have?

More than they did a week ago. Until now, the argument that couples should wait until they are married before they have sex has rested on mere assertion and anecdote. Dean Busby and his colleagues at Brigham Young University, in Utah, however, have gathered some data which support delay (conveniently for the university, which is owned by the famously abstinent Mormons).

Fabian tactics

Little is known about the influence of sexual timing on how relationships develop. Even so, opinions abound. Some argue that the sexual organs, both physical and mental (for, as the old saw has it, the most powerful erotic organ is the mind) need a test drive to make sure the chemistry between a couple means they will stay together both in sickness and in health. Others suggest that couples who delay or abstain from sexual intimacy early on allow communication to become the foundation of their attraction, and that this helps to ensure that companionship and partnership keep them together when the initial flames of lust die down.

To examine these suggestions more closely, Dr Busby and his colleagues recruited 2,035 married people ranging in age from 19 to 71, and in length of marriage from less than six months to more than 20 years. Their religious affiliations varied widely; many had none.

All were asked to complete an online questionnaire normally used to help couples understand their strengths and weaknesses. Among the nearly 300 questions, participants were asked when they first had sex with their partners, whether their sex lives were currently good, how they resolved conflicts, and how often they thought of ending their relationship. In addition, the questionnaire had 14 items that evaluated how good participants were at expressing empathy and understanding to their partners and how prone they were to be critical or defensive. All questions, apart from those about frequency of sex, were answered on a five-point scale, with one indicating strong disagreement and five indicating strong agreement.

Pleasure deferred?

The association between time of consummation of a relationship and subsequent marital harmony

1=worst, 5=best

Timing of first sexual intercourse	Women		Men	
	Early on	After marriage	Early on	After marriage
Communication	3.5	4.0	3.4	3.9
Sexual quality	3.3	3.7	3.4	3.8
Relationship satisfaction	3.0	3.7	3.2	3.8
Perceived stability	3.6	4.3	3.7	4.4

Source: Busby et al, *Journal of Family Psychology*

Because religiosity delays sexual activity, Dr Busby and his colleagues also asked participants how often they attended church, how often they prayed and whether they felt spirituality was an important part of their lives. They used the answers to control for religiosity. They also controlled for income, education, race and length of relationship.

Their report, just published in the *Journal of Family Psychology*, suggests that people who delay having sex do indeed have better relationships, on four different measures (see table). That result applies to both men and women.

Unfortunately, Dr Busby's method cannot distinguish the cause of this. It could be, as many moralists preach, that the delay itself is improving. It could, though, be that the sort of people who are happy to delay having sex are also better at relationships. Correlation, in other words, rather than causation. That is material for another study. If the result persists, though, even when personality is taken into account, it will provide useful ammunition for priests and marriage-guidance counsellors.

Index | Science & Technology

Planetary rovers

Space hopping

Jan 20th 2011 | *CAMBRIDGE, MASSACHUSETTS* | from PRINT EDITION

How to bounce across a planet's surface



Life on Mars?

ROBOT vehicles which drive across a planet's surface have proved a great success. *Spirit* and *Opportunity*, two solar-powered rovers that landed on Mars in 2004, were built for a mission intended to last 90 days. *Spirit*, though, kept going until it got stuck in sand in 2009-and *Opportunity* is still motoring, having now clocked up more than 26km (16 miles). They are not, however, perfect. Besides being slow (top speed 0.2kph) and at risk of sand traps, wheeled rovers like *Spirit* and *Opportunity* have other limitations. They cannot, for example, cross rocky terrain or ravines. But a new type of exploration vehicle, called *Talaris,* should be able to get round such problems. Or, rather, over them. For it is, literally, a space hopper.

Sadly, it looks nothing like the famous toy from the 1970s. Instead of a friendly orange blob, it resembles something that has escaped from a medieval torture chamber. It is the brainchild of a group led by Bobby Cohanim at the Draper Laboratory, an independent research centre in Cambridge, Massachusetts. Students from the nearby Massachusetts Institute of Technology are also working on the vehicle, which is due to attempt its first hop outside a laboratory this spring.

Mr Cohanim describes the way *Talaris* moves as a "hover-hop". First the machine takes off and hovers above the ground by firing downward-facing nozzles. (These use nitrogen for the moment, but that will be replaced by a higher-energy rocket system if the vehicle is actually deployed on another planet.) It then hops to its destination by directing some of the gas to sideways-facing thrusters, to propel itself backwards or forwards. Once it has arrived, the strength of the hovering jet is reduced until it lands.

A novel part of the design is a second propulsion system that simulates low-gravity environments. This allows *Talaris* to be test-flown as if it were on, say, the moon. (The hopper's name is a contrived acronym of Terrestrial Autonomous Lunar Reduced Gravity System). This second system consists of four ducted fans, one mounted at each corner of *Talaris*'s carbon-fibre frame. By blowing downward these fans oppose the force of gravity, effectively lightening the vehicle. To simulate a mission on the moon, they would blow hard enough to reduce the weight of *Talaris* by about five-sixths, as the moon has only a sixth of the gravity found on Earth.

The group developing *Talaris* are members of Next Giant Leap, one of the teams competing for Google's Lunar X Prize. This will award $20m to the first privately financed team to land a robotic vehicle on the moon, travel 500 metres on the lunar surface, and send pictures and data from the enterprise back to Earth.

Although *Talaris* is designed to try to win the X Prize, it could also be used to explore planets like Mars-and possibly asteroids too, according to Seamus Tuohy, Draper's director of space systems. Apart from avoiding hazards and rough ground, it would be able to jump into the bottom of a crater or ravine to analyse samples and take photographs, and then jump out again. It could also hover down a cliff face to examine geological strata.

Unlike a solar-powered wheeled rover, a space hopper's endurance will be limited by the amount of fuel it can carry. Nevertheless, Dr Tuohy believes hoppers will compliment wheeled rovers, because they will be able to cover much more ground. They will also be able to boldly go where no rover has gone before.

Cigarettes in films

Smoked out

Jan 20th 2011 | from PRINT EDITION

Can a film of a smoker trigger the act?



The mirror cracked from side to side

FOR beleaguered smokers, the world is an increasingly hostile place. Hounded out of bars and other public spaces, tutted at in doorways and shelters, smokers are now to be found cowering down cold and smelly alleyways. To add to their misery, each day seems to bring a new study showing how vile and dangerous even a whiff of cigarette smoke can be. Could things get any worse?

Possibly, if smokers were also knocked off their comfortable perch within popular culture. For smokers in rich countries have at least been able to rely on films (especially, but not only, classic ones) to portray their habit as somewhat more normal and prevalent than it actually is in the real world. Indeed, Hollywood has long been accused of glamorising smoking, and thereby encouraging people to emulate their on-screen idols.

Research has identified links between smoking in films and the consumption of cigarettes by those leaving a cinema. What prompts such a response is unclear. But it is clearly relevant to those involved in public-health policy. Dylan Wagner and his colleagues at Dartmouth College, in New Hampshire, therefore decided to investigate the question.

They put 34 people, half of them smokers, into a functional-magnetic-resonance imager. Such machines detect changes in the blood flow in various parts of the body-in this case, the brain. In that organ, such changes correspond to increases and decreases in mental activity. Magnetic-resonance imagers are thus, in a manner of speaking, a way of reading minds and are therefore as beloved by advertisers as by neuroscientists.

Participants were asked to watch the first 30 minutes of "Matchstick Men", a film about con men chosen because it features many smoking scenes but lacks scenes showing the possibly confounding variables of alcohol use, violence and sex. As in many such research projects, participants were misled over the nature of the study and were not aware that it was about smoking. The results are reported in the *Journal of Neuroscience*.

When smokers viewed a scene that included smoking, they showed greater activity in those parts of the brain involved in perception and in the co-ordination of actions-the areas known to interpret and plan hand movements-as though they, too, were about to light a cigarette. This activity also corresponded to the hand that the volunteer used when smoking. Non-smokers showed no such enhancement.

The part of the brain affected is the home of what is known as the mirror system. This induces, from mere observation, emotions and sensations similar to those induced by actual experience-for example, fear when a large spider is climbing the leg of an actor in a film. That it might provoke a desire to smoke is thus no surprise.

Scott Heuttel, a neuroscientist at Duke University, in North Carolina, says that it has long been known that visual cues induce drug cravings, and that this study builds on a growing body of evidence showing that addiction may be reinforced not just by the drugs themselves but by images and other experiences associated with those drugs. Although smokers trying to quit are advised to avoid other smokers, and to remove smoking-related paraphernalia from their homes, it might not occur to them to avoid films in which smoking is depicted.

No doubt, though, it will occur to society's nannies to remove the temptation altogether. Expect, on the basis of findings like this, a drive to purge films of characters who smoke. Unfortunately for smokers there is, as a gravelly voice-over might say in Hollywood, "No Place to Hide".

Index | Science & Technology

Water purification

Any old iron?

Jan 20th 2011 | from PRINT EDITION

A little-known chemical may provide a new way to clean water

IRON in water is normally regarded a pollutant. Luke Daly, the boss of Ferrate Treatment Technologies of Orlando, Florida, however, plans to turn that thought on its head. He intends to use a chemically unusual form of iron to clean water up, not make it dirty.

Iron is found in the part of the periodic table known as the transition metals. Like all metals, these react with other elements by giving up electrons to form positively charged ions. Transition metals, though, give up different numbers of electrons in different circumstances, and thus have ions of various charges. Usually, iron loses two or three electrons. But in ferrates, which are compounds of iron and oxygen with non-transition metals like sodium and calcium, it loses six. That makes ferrates extremely reactive, and it is this reactivity which Mr Daly hopes to exploit.

First, ferrates are strong oxidising agents. That means they destroy bacteria and viruses, and break up organic molecules with alacrity. Second, they are coagulants and flocculating agents. They attract other chemicals in the water, including dissolved metals, and precipitate them for easy removal. Moreover, once it has done its job, the iron in ferrates precipitates too, as iron oxide, leaving pure water behind.

The reason these wonder materials have not been used as water purifiers before is that their reactivity makes them unstable and thus difficult to store. Thomas Waite of the Florida Institute of Technology, an academic scientist on whose work the company has drawn, jokes that in the early days of his research he kept the whole world's supply of ferrates in a cabinet in his laboratory.

Ferrate Treatment Technologies' trick is to make ferrates on site, for instant use, rather than attempting to transport them to where they are needed. The firm's "Ferrator" uses three cheap raw materials-bleach, ferric chloride and caustic soda-to produce sodium and calcium ferrate at a price competitive, in terms of oxidising power, with more familiar water-cleaners like chlorine and ozone.

A machine small enough to be carried around in a pickup truck, Mr Daly claims, could generate enough ferrates to purify 75m litres (20m American gallons) of water a day. The system is now being tested at two plants in Florida. If all goes well, the first commercial Ferrators will be up and running later this year.

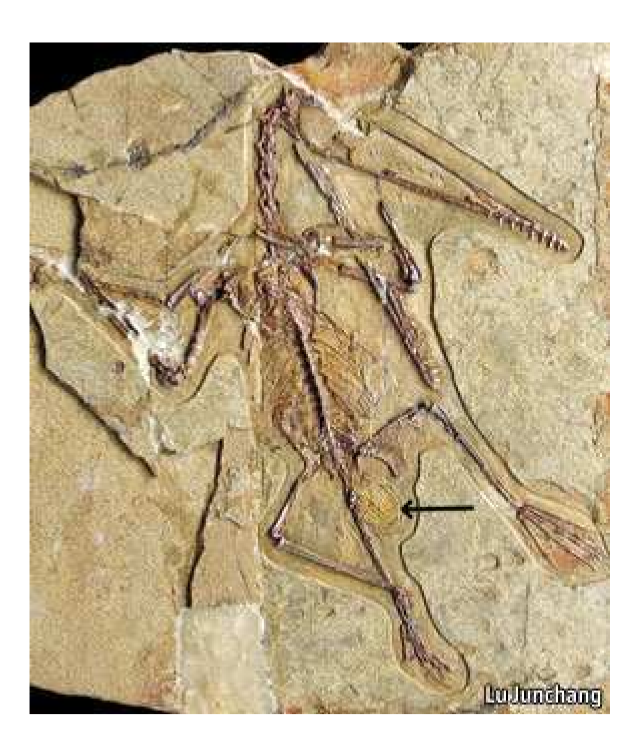
Index | Science & Technology

Palaeontology

Unscrambled eggs

Jan 20th 2011 | from PRINT EDITION

An insight into the lives of pterosaurs



THE photograph right shows a fossil pterosaur (an extinct flying reptile) called *Darwinopterus*. The fossil itself is in Zhejiang Museum of Natural History, in Hangzhou, China, and was found in the mid-Jurassic strata of Lianong province. It has just been described by Lu Junchang of the Chinese Academy of Geological Sciences, in Beijing, and his colleagues in a paper in *Science*. What is remarkable is the feature marked with an arrow, an egg. That both identifies the specimen as female and casts light on how pterosaurs reproduced.

Until recently the assumption was that, like birds, pterosaurs looked after their hatchlings in nests. This specimen suggests that is not true. The egg seems designed for burial rather than for the nurturing embrace of a mother pterosaur. Its outer layer is parchmentlike, which is characteristic of the ova of modern egg-burying reptiles such as turtles. Just as baby turtles can swim as soon as they have hatched, this find suggests that baby pterosaurs-of this species, at least-could fly.

The specimen also helps confirm the previously unproven belief that *Darwinopterus* was sexually dimorphic, with the males sporting crests and the females lacking them. Both crested and crestless specimens are known, but this one suggests crestlessness was a female trait. This is no great surprise, since it is usually the male of any dimorphic species who is encumbered with any expensive ornamentation. But it is a nice confirmation that Darwin's observations about sexual selection being a matter of males showing off to females were as true 160m years ago as today.

Modern India

Over a billion people now

Jan 20th 2011 | from PRINT EDITION

A colourful depiction of momentous times in a giant country

India: A portrait. By Patrick French. *Allen Lane; 436 pages; pound25. To be published in America by Knopf in June; $30.* Buy from Amazon.com, Amazon.co.uk



ONE of the startling features of India's economic progress is how much opposition it stirs at home. Across the political divide, many people are still sceptical of the two-decade-old reform programme that underpins the boom, including leading lights of the ruling Congress party. Their gripes are often rhetorical-even India's communist parties have grudgingly embraced capitalism in the three states where they rule. But critics still need to be reminded how badly India was served by its former mixed economy.

Patrick French, a British writer and historian, performs that service in his new book, "India: A Portrait". In an admirable chapter on India's early efforts at central planning, he describes the thinking of Jawaharlal Nehru, India's first prime minister, as a "Keynesian idea of a mixed economy taken to extremes that Keynes would have found fiscally impossible". Largely through government spending, newly independent India sought to increase industrial output fivefold and double incomes per head within 15 years. Its supremely optimistic planners then went on wasteful splurges in heavy industry, brought in innumerable laws to promote cottage enterprises and imposed barriers to imports and exports.

By the time of Nehru's death in 1964, India's share of world trade had halved. His daughter, Indira Gandhi, who succeeded him, then prescribed an even bigger economic role for the state, and the waste and mismanagement spiralled. In 1978 Coal India, a state-owned giant, lost $258m-more than the total earmarked for government welfare spending in the entire five-year plan of that time.

Such losses contributed to the 1991 balance-of-payments crisis. With less than $1 billion in reserves, India was forced to export gold to stave off bankruptcy. In desperation, Manmohan Singh, an economist and bureaucrat, was appointed finance minister and implored to do something. With a forthrightness for which he has never otherwise been known, Mr Singh promptly tore down many of the controls. He slashed tariffs, abolished licences and allowed foreign investment to

flow in. India's economy, with one or two splutters, took off. Last October, in its biggest initial public offering so far, the government, now headed by Mr Singh, sold 10% of Coal India for around $3.5 billion.

It is a testament to India's rise that serious guides to the country, like Mr French's, now devote as much space to business and the economy as to Indian politics, culture and religions. Once seen as unchanging, or unsalvageable, India is now widely recognised as a dynamic, innovative, soon-to-be economic powerhouse. And Mr French, a devotee of South Asia, is good on the other stuff, too. In distinct sections on politics, the economy and society, he typically gives some essential history, and then a rich colouring of contemporary characters and events, many of them sharply observed at first hand. The book is crammed with elegant portraits of important Indians, brilliant Indians, wretched Indians, and hilarious Indians like the septuagenarian Dr K. Chaudhry, who recorded himself murdering hundreds of well-known pop songs, posted them on YouTube, and became an overnight internet star.

But this can also get a mite tedious. Amid his myriad observations, Mr French offers little in the way of fresh analysis, and some that is too thin. He is too kind to the latest Nehru-Gandhi rulers, for example. Sonia Gandhi, Congress's leader, has been much more successful than anyone had predicted, but that does not make her the shrewd strategist of Mr French's description. And though it is true that her son and Mr Singh's expected successor, Rahul, speaks sparingly in public, this is probably as much due to his diffidence as to the far-sighted inscrutability that Mr French sees in him. The Gandhis and Mr Singh also deserve more opprobrium than Mr French dishes out for the corruption and crude populism of India's recent governments.

While presenting few new ideas, Mr French has a sometimes surprising tendency to lay claim to established ones. That Western power will be diminished in relative terms by Asia's rise, that Indian politics is becoming ever more dynastic and that the country's Hindu nationalists need to freshen up their manifesto are all commonplace. Mr French suggests them as insights. Meanwhile he decries lazy journalists who "make a living by reporting ceaseless tales of woe" from India; but these are a dying lot. In recent years, foreign reporting of the country has often gone too far the other way, lauding India's economic growth with only occasional easy-to-spot regard to the country's manifold problems.

Mr French is a fine reporter, with an appealing fascination for all things Indian, as his book makes clear. Despite its flaws, it is an accomplished portrait of momentous times in a remarkable country.

Pakistan

Future unrosy

Jan 20th 2011 | from PRINT EDITION

Was Partition always going to be violent?

Tinderbox: The Past and Future of Pakistan. By M.J. Akbar. *HarperCollins India; 343 pages; 499 rupees*



Jinnah, patrician and partisan

WHEN India and Pakistan began, in 1947, they shared many of the same peoples and a legal and administrative history going back five centuries. What explains their subsequent divergence, with India now broadly stable and prosperous and Pakistan crisis-ridden? According to M.J. Akbar, an erudite Indian journalist who is a Muslim, "The idea of India is stronger than the Indian; the idea of Pakistan is weaker than the Pakistani."

India was founded as a secular democracy. Given its great diversity, it is hard to think how it could have been otherwise. Pakistan was created to be a homeland for India's Muslims, an idea that was weak on two counts. First, because it implied a threat to Muslims, or Islam, in Hindu- majority India that in retrospect appears bogus. India's 160m Muslims are free and no worse off than Pakistan's 180m. Second, the Islamic rationale for Pakistan contained an ambiguity about the role of Islam in the new state, which has given rise to extremism. As Mr Akbar writes, "the germ of theocracy lay in Pakistan's genes."

No one would have been more appalled by this than Pakistan's founder, Muhammad Ali Jinnah. A whisky-drinking anglophile, he envisaged Pakistan as an India-style democracy. Yet he also helped begin its descent by playing upon chauvinist Muslim fears for political gain. A stalwart of the independence movement, he had been a late convert to the cause of Pakistan, swayed to it only after the early collaboration between Hindu and Muslim freedom-fighters had broken down.

There were many reasons for this. Indian Muslims had a history of violent opposition to the British that was at odds with Gandhi's non-violence. Their elite felt superior to Hindus-a hangover from the Mughal empire-and feared losing their residual privileges under Hindu rule. The leaders of the Congress party, including Jawaharlal Nehru, were insensitive to these fears. It also suited India's British rulers to worsen the schism. Had any of these parties acted differently, the calamity of partition, in which perhaps a million perished, might perhaps have been avoided.

Among many recent books on Pakistan, Mr Akbar's stands out. Above all, it is a fine and detailed history of Indian Muslim anger and insecurity, spawned by the 18th-century decline of the Mughals, and the way this played out in the freedom struggle. It is a lively read; Mr Akbar is a stylish writer with an excellent eye for a gag. Of the Mughal emperor Babur, he writes, he "was equally adept at writing poetry, art criticism, military strategy and piling rebel skulls in the shape of a pyramid."

The book's final chapters, on Pakistan's recent struggle with militancy and extremism, are less good. That may have to do with Mr Akbar's nationality. Denied much access to Pakistan, Indian analysts sometimes struggle to keep abreast of it. But that Mr Akbar is Indian, let it be said, is largely immaterial: his book is fair and balanced. So, too, were his opening remarks at its launch, attended by an array of Indian leaders. "If Salmaan Taseer had been an Indian Muslim, he would be alive today," he said, referring to the Pakistani governor of Punjab, murdered by a fanatic this month. That was provocative; also true.

The rise and fall of the dollar

Go with the flows

Jan 20th 2011 | from PRINT EDITION

Lessons of history

Exorbitant Privilege: The Rise and Fall of the Dollar and the Future of the International Monetary System. By Barry Eichengreen. *Oxford University Press; 224 pages; $27.95. To be published in Britain by OUP next month; pound14.99.* Buy from Amazon.com, Amazon.co.uk



THE dollar's ascendance to the rank of world's most important currency is often remembered as having been slow and gradual, mirroring the decline of sterling and Britain's historic economic dominance. In fact, it was surprisingly swift. From a standing start in 1914, the dollar had overtaken sterling in international importance by 1925. The first world war played a part, but so did a lesser-known factor. America had surpassed Britain as the world's largest economic power as early as 1870, but it had a stunted financial system: its banks could not open branches abroad, it had no central bank and panics were common. All these things discouraged international use of the dollar.

This began to change with the creation of the Federal Reserve in 1913, providing stability to the American banking system. Benjamin Strong, the Fed's *de facto* leader in its early years, saw how the deep and liquid market for trade acceptances-the IOUs that were used to finance shipments of goods-helped the Bank of England to manage credit conditions. The Fed used its clout to nurture a similar market in America. This hastened the migration of international financial activity from London to New York, and from sterling to the dollar.

Whether the dollar will share sterling's fate is a common question in geopolitical circles. After all, it is only a matter of time before China's GDP overtakes America's. But as Barry Eichengreen shows in a fascinating and readable account of the dollar's rise and potential fall, reserve-currency status depends on far more than GDP. It is also a function of strategic and military relationships, laws, institutions and incumbency.

Mr Eichengreen, who teaches at the University of California, Berkeley, is an international monetary historian whose research into how the gold standard propagated the Great Depression was the basis for his seminal 1992 book, "Golden Fetters". His latest work is less about the future of the financial system than its history, and skilfully told history it is too. Mr Eichengreen sprinkles his economics with memorable sketches of economic and political leaders. Jimmy Carter, apparently, handicapped his efforts to reduce Germany's trade surplus by addressing the more formal Helmut Schmidt, the German chancellor, by his first name.

The book's title was inspired by Valery Giscard d'Estaing, France's finance minister in the 1960s, who once described the enormous benefit America derived from the dollar's reserve status as its "exorbitant privilege". The world's need for dollars lets America borrow at lower cost. American companies are spared the hassle of transacting in another currency. Those suitcases of dollars so beloved of international arms smugglers and drug kingpins all represent interest-free loans to America.

That the world remains so dollar-centric, given America's shrinking share of world output, is something of an anomaly. This could be explained for most of the post-war period by lack of competition. Japan discouraged international use of the yen for fear of elevating its value and hurting its exports. The presence of the Red Army on West Germany's borders hung over the Deutschmark, and in any case Germany regarded support of the dollar as an intrinsic part of its military alliance with America.

Mr Eichengreen does not think the dollar is about to be vanquished as sterling was. Rather, he foresees a "multipolar" system of international currencies. Reunification shifted Germany's priorities from supporting America to binding itself more closely to Europe, resulting in the creation of the first significant competitor to the dollar, the euro. Mr Eichengreen could have devoted more attention to the strains that Europe's sovereign-debt crisis have placed on the euro. His book is optimistic, noting that political rather than economic imperatives have always driven the euro. Mr Schmidt sold monetary integration to Germany's sceptical central bank by invoking Auschwitz. Yet Mr Eichengreen's recent writings betray a pessimism about the euro's future that is not visible in his book.

And what of China? As was true of America and the dollar a century ago, China's currency does not enjoy anywhere near the clout that could be expected from the size of the Chinese economy. As with Japan, China has discouraged internationalisation of its currency for fear that inflows of capital would lift its value and curb Chinese exports. It has learned, however, from Japan's mistakes, and is gradually liberalising the use of its currency. But China is still much further behind than America was in 1914; it will be decades before the yuan rivals the dollar's leadership.

The chapter on the international financial crisis is an unsatisfying rehash of the usual explanations, such as loose monetary policy, sloppy underwriting and derivatives. Mr Eichengreen underplays the role that China played, through its accumulation of dollars, in financing America's housing bubble. He thinks the crisis will accelerate the shift to a multipolar currency system, but that the dollar will not collapse. That would take profound economic mismanagement by America itself, in particular, unchecked budget deficits. It was Britain's dismal economic performance, not the dethronement of sterling, that cost it its great-power status after 1945. "The only plausible scenario for a dollar crash", Mr Eichengreen concludes, "is one in which we bring it upon ourselves."

Index | Books & Arts

Economic folly

How the reader was lost

Jan 20th 2011 | from PRINT EDITION

How the West Was Lost: Fifty Years of Economic Folly-and the Stark Choices Ahead. By Dambisa Moyo. *Farrar, Straus and Giroux; 226 pages; $25. Allen Lane; pound14.99.* Buy from Amazon.com, Amazon.co.uk

HERE are two predictions about the world economy. First, the West's malaise and the rise of emerging economies will yield a mountain of books. Second, few of these are likely to be as bad as "How the West Was Lost".

Dambisa Moyo, a Zambian-born economist whose provocative first book attacked foreign aid in Africa, accuses the West of squandering the sources of its economic growth. Borrowed money has been poured into unproductive uses, notably housing. Its workers are ageing or, if young, dream of being footballers or fund managers rather than engineers. Technology has been handed to, or stolen by, the Chinese. Government policies over half a century have encouraged or abetted all this. Unless the West changes its ways, it is heading for "a savage economic decline".

Much of this is both plausible and familiar. The trouble starts when Ms Moyo ventures into economic analysis. In comparing America's economy with China's, for instance, whether you convert yuan into dollars at market exchange rates or after adjusting for purchasing power matters a lot. Measuring at purchasing-power parity makes the gap in GDP and living standards look narrower. This explains a great deal of the difference between two sets of figures that Ms Moyo cites. Yet she does not mention it.

This is basic stuff. Much else in elementary economics also gets mangled here. Governments usually manipulate exchange rates to make their currencies artificially weak, not strong. In the Keynesian national-income identity, G represents government spending, not the budget surplus. The idea of a special tax on sports stars' incomes to discourage youngsters from unrealistic aspirations is intriguing, if contentious; suggesting that the two groups might bargain away such effects is absurd.

There are some puzzling omissions. Ms Moyo rightly complains at the exclusion of big emerging economies (except Russia) from the G8. She celebrates the strengthening of their diplomatic muscles. Amazingly, she seems not to have noticed the prime manifestation of this: the rise of the G20, which since 2008 has eclipsed the smaller, rich-country club.

Worse, Ms Moyo commits some jaw-dropping factual errors. General Motors, she writes, was bought by Fiat, "an event unimaginable just a couple [of] years earlier". Yes, and it still is: the Italian carmaker did not purchase GM, but a 20% stake in Chrysler, recently increased to 25%. France gets "almost 20% of its electricity from nuclear sources". The OECD says the figure is close to 80%.

Ms Moyo's editors are as bad as her fact-checkers. If they couldn't spot the analytical flaws, they might have done something about the stylistic ones that range from curious analogies to long phrases in parentheses. Endnotes are used almost at random.

The book ends with some provocative claims. America's indebtedness and crippling health-care and pension burdens, Ms Moyo believes, may lead it to create a "socialist welfare state" by the latter part of the century, or to default on its public debt. Should the world descend into autarky, America would be better equipped than China for survival on reduced means. But these arguments need much better supporting material than the book provides. By that stage the reader's trust in the author will already, so to speak, have gone south.

Index | Books & Arts

The global economy

Forecasting trouble

Jan 20th 2011 | from PRINT EDITION

Looking ahead in the dark

Outrageous Fortunes: The Twelve Surprising Trends That Will Reshape the Global Economy. By Daniel Altman. *Times Books; 272 pages; $25 and pound18.99.* Buy from Amazon.com, Amazon.co.uk

SAMUEL GOLDWYN is one of several people believed to have said, "never make forecasts, especially about the future". Daniel Altman, an American academic economist who once worked for *The Economist*, blithely ignores this advice in his new book. Indeed, he offers no fewer than 12 big predictions for what he calls the "deep factors" that will most affect the future of the world economy.

This is a bold exercise and, albeit fitfully, an interesting one. The author rightly complains that too much forecasting, not just in economics, is short-termist, looking a year or two ahead at most. It also tends to be linear: too often forecasters merely project forward recent trends. It is also clear that people tend to overestimate the immediate impact of new developments but underestimate their longer-term effects.

Mr Altman writes with some verve, yet he makes only a partially convincing case in support of his predictions. He is best on purely economic ones. Thus he is surely right to argue that China's seemingly inexorable growth will slow, though it is less clear that China may, like Japan before it, then slip back. He is also persuasive in maintaining that the rich world's policies on immigration (taking in the brightest and best) and the environment (transferring polluting industries abroad) will damage the poorest countries.

But he is on weaker ground in many of his broader forecasts. The suggestion that the future, like the past, will belong to the middleman may suit his view of America as the world's salesman, but it sits ill with many other signs of disintermediation. The argument that a motley group of "lifestyle hubs", including Bulgaria and even Tunisia of all places, will take over from the likes of London, New York and Paris as the favoured bases for the rich and successful seems fanciful.

Mr Altman is also cavalier in forecasting the demise of several of the world's international institutions. In truth, it takes a lot to overcome natural inertia and kill any organisation. Predictions that the European Union will disintegrate economically and that the World Trade Organisation will also collapse give too little weight to the value placed on these bodies by their present and prospective members. Several countries in eastern and south-eastern Europe are eager to join the EU and even the euro; and Russia is not the only country aspiring to get into the WTO. How effective these organisations will be may be debatable, but it seems decidedly premature to write their obituaries.

Overall, the tone of Mr Altman's book is strikingly gloomy about the future, except oddly for that of his own country. In the longer-term perspective that he favours, the gloom seems excessive. In a 1930 essay on "Economic Possibilities for our Grandchildren", John Maynard Keynes mused on a future 100 years thence, when much of humanity would have solved the perpetual economic problem of subsistence. At least in rich countries, that future is likely to be realised, as Keynes predicted, by about 2030. Keynes's vision of a cultural and intellectual paradise may have been naive. But Mr Altman would do well, perhaps in a second edition, to explore not just potential problems but also the effects of undreamed-of levels of prosperity, at least in Europe and America.

Index | Books & Arts

Ibsen's "John Gabriel Borkman"

Winter chill

Jan 20th 2011 | *NEW YORK* | from PRINT EDITION

A new production of a rare and all-too-relevant play



Corseted and suffocating

HENRIK IBSEN understood the cloying power of the sumptuous drawing room. The heavy furniture and stale air, the binding corsets and suffocating mores; what could be more maddening? In such cosy prisons minds don't merely wander, they race. So it is with "John Gabriel Borkman", Ibsen's penultimate play, about a disgraced former bank manager who pads around like "a sick wolf" in the cage of his home. Jailed for years, he now sulks in his study while his aggrieved wife prowls around downstairs. The action takes place on a single winter evening in rooms as frigid as the surrounding snow.

Anyone who sees the Abbey Theatre's production, now at the Brooklyn Academy of Music, will wonder why this play is not staged more often. It is not just that the 19th-century drama feels timely; it concerns a cocky man who misused other people's money. In the right hands, as in this version directed by James Macdonald, "John Gabriel Borkman" tells a deeper story about the desperate ways people try to make sense of their lives. Too miserable to comprehend the present, the characters cling to false memories and delusional expectations. "Castles in the air-they are so easy to take refuge in," Ibsen once observed.

Tom Pye's elegant set mixes shiny dark surfaces with stark white snow. The colour comes from the performances. A grand cast, working from a new translation by Frank McGuinness, features Alan Rickman as the titular banker, Fiona Shaw as his vengeful wife and Lindsay Duncan as her estranged sister and his betrayed lover-a fiercer trio can hardly be found on the modern stage. The tricky roles veer close to melodrama, but these actors find their humanity, and deliver tension to scenes that might otherwise feel overlong.

Lonely and dying, Ella (a dignified and restrained Ms Duncan) pays a surprise visit to her family's estate. She hopes to convince her nephew, Erhart, to live with her again. But her twin sister, Gunhild, who is Erhart's mother, has other plans for the young man. Hobbled by the "filthy disgrace" of her husband's crimes and righteous in her innocence ("How could I know it wasn't his own money he gave me to squander?"), she clings to Erhart in the belief that he will clear the family name. In Ms Shaw's hands, Gunhild is no one-note harpy. Limping about and brimming with noxious anger, she makes it difficult to look elsewhere on stage.

Mr Rickman makes for a delicately grim Borkman. Abandoned yet impenitent, he spends his days brooding and waiting for the day he will be vindicated. Though he never goes out, he is dressed immaculately, from his cravat to his shiny shoes, ever prepared for when his bank colleagues "come up here, get down on bended knees and beg me to come back", he says in that dark-chocolate voice of his. Seduced by power, he tossed aside his love for Ella in order to create the kingdom of his dreams. Now he is bankrupt and loveless, with only his delusions to keep him going. "Isn't it a very mysterious thing-human happiness-how it works out?" asks Borkman's lone friend, a humble poet. Mysterious indeed, especially for these unhappy souls.

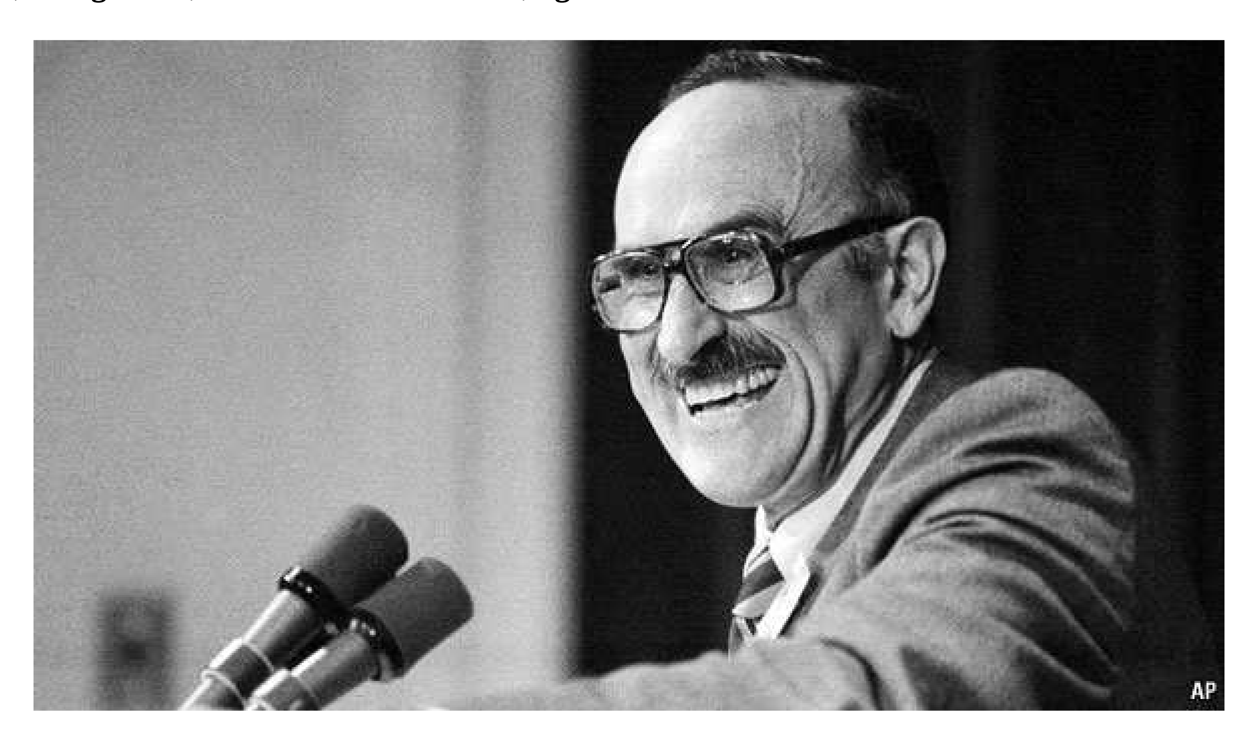
"John Gabriel Borkman" is at the Harvey Theatre, Brooklyn Academy of Music, until February 6th

---

Alfred Kahn

Jan 20th 2011 | from PRINT EDITION

Alfred Kahn, deregulator, died on December 27th, aged 93



WHEN everyone else at the airline counter for the flight from Hicksville to Washington was sighing, checking their watches and using their elbows on their neighbours, Alfred Kahn would be smiling. And later, cramped in his seat between some 20-stone wrestler and a passenger whose "sartorial, hirsute and ablutional state" all offended him, snacking from a tiny packet of peanuts that had cost him a dollar, he would sometimes allow the smile to spread under his Groucho Marx moustache into a big, wide, gloating grin.

For Mr Kahn had made this crowd and packed this aircraft. His deregulation of America's airlines in the 1970s opened up the skies to the people, for better and worse. And though, being an economist, he could not help muttering about the imperfection of societies and systems and the absurdity of predictions-and though, being an inveterate puncturer of himself, he would demand a paternity test if anyone called him the father of the deregulated world-his adventures with airlines led on to the freeing of the trucking, telecoms and power industries, and heralded the Thatcherite and Reaganite revolutions.

When he took over the Civil Aeronautics Board for President Jimmy Carter in 1977 air travel was regulated to the hilt, with prices, routes and returns all fixed and aircraft, which could compete only on the number of flights and the meals they served, flying half-full. Mr Khan, furiously resisted by companies, pilots and unions, removed the rules. As an academic, author of "The Economics of Regulation" in two stout volumes, he was eager to see those elusive and fascinating things, marginal costs, brought into play: to let prices follow the constantly shifting value of an aircraft seat as demand changed or departure time loomed, or indeed as shiny new jet planes depreciated above him, just "marginal costs with wings".

He had no idea what would happen when he took the restraints off, except that, at a time of raging inflation, he was pretty sure fare prices would fall. The great wave of mergers, predations and bankruptcies that followed shocked him; the reconcentration of the industry into giant hub-and-spoke operations scandalised him; the disappearance of the humble Allegheny Airlines flight that used to take him to work, transformed into USAir's transcontinental ambitions, annoyed him; but he could only be delighted that by 1986 90% of Americans were flying on discounts, and that the savings to consumers were reckoned at around $20 billion a year.

His success was all the more surprising because he was an old-fashioned Democrat, from his shiny pate to the stockinged feet in which, like a lizard, he would pad around the office. (His party piece was Stephen Sondheim's "Send in the Clowns", dedicated to the Reagan administration.) Yet his thinking had scarcely a shred of Keynesianism in it. Mr Kahn sometimes talked wistfully of price caps, especially when he was appointed Mr Carter's "inflation tsar" in 1978, a

thankless, staffless, hopeless job which he threw in after 15 months, inflation riding high as ever, declaring that no one else would be fool enough to do it. But politics always ran second to economics, and his economics was the classical kind, in which everything was left to the markets. The government, if it couldn't be useful, should get the hell out of the way. And this, as a federal bureaucrat, he did, enthusiastically undermining his own agency until it ceased to be.

A fruit substitute

Really, he said, he was a show-off and a ham; he loved the spotlight, and if he hadn't been such a brain at school and college, steaming effortlessly (if short-sightedly) towards the economics department at Cornell, he would have gone in for musicals. The songs of Cole Porter and Irving Berlin were on his lips, as well as numbers from "The Pirates of Penzance" and "The Yeoman of the Guard", in which he sang and danced until his 80s.

Breezily, too, he winged his way in government. He was an academic, after all; he had nothing to lose, so he would speak his mind. Asked once by a reporter if he could defend the defence budget, he said "No". Told off for using the word "depression" in public, he replaced it with "banana", and announced that the country was heading for its worst banana in 45 years. Told off by the head of United Fruit for using "banana", he made it "kumquat". As the oil price continued to soar he called the Arab producers "schnooks", earning yet another rebuke; but he didn't care. He could always go back to being dean of Cornell's College of Arts and Sciences, as he did in 1980, even though "dean is to faculty as a hydrant is to a dog."

His great passion was to set things free: not just the airlines, not just his own wickedly candid tongue, but also the English language. In a famous memo at the start of his stint at the CAB he begged staff to write drafts as if they were destined for their children or their friends; to eschew "herein" and "regarding" and "prior to" in favour of "here", and "about" and "before". Away with gobbledygook and pomposity, though "a final example of pomposity, perhaps, is this memorandum itself." No airs and graces, and preferably no "Alfred" either: just Fred, jetting here and there, round and about, with his discount ticket and his warm, wide, proud, unstoppable smile.
